THE BULGARIAN ECONOMY

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THE CENTER FOR ECONOMIC DEVELOPMENT

Editors in charge: Alexander Boshkov, George Prohasky Ph.D., Ivaylo Nikolov

This report was prepared by: Anelia Damianova Ph.D., Blenika Djelepova, Daniela Petrova, Elena Pavlova, Georgi Mihaylov, Ivaylo Nikolov, Jana Spassova, Liliana Doudeva, Magdalena Varshilova, Maria Prohaska Ph.D., Marieta Tzvetkovska, Petar Stankov, Stanislav Slavov, Zdravko Ivanov

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1408 Sofia, 1 Balsha St., bl. 9
e-mail: aeconomy@ced.bg

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CONTENTS

ABBREVIATIONS USED

AD.......................... JOINT-STOCK COMPANY
AEAP...................... AGENCY FOR ECONOMIC ANALYSIS AND PROJECTIONS
AISFC.................... AGENCY FOR INTERNAL STATE FINNCIAL CONTROL
ASME.................... AGENCY FOR SMALL AND MEDIUM- SIZED ENTERPRISES
BAS....................... BULGARIAN ACADEMY OF SCIENCE
BASSCOM............. BULGARIAN ASSOCIATION OF SOFTWARE COMPANIES
BDU....................... BULGARIAN DOCTORS' UNION
BIA......................... BULGARIAN INDUSTRIAL ASSOCIATION
BNB....................... BULGARIAN NATIONAL BANK
BNR....................... BULGARIAN NATIONAL RADIO
BNT....................... BULGARIAN NATIONAL TELEVISION
BRS....................... BULGARIAN RIVER SHIPPING
BTC....................... BULGARIAN TELECOMMUNICATIONS COMPANY
CB.......................... CENTRAL BUDGET
CEE....................... CENTRAL AND EASTERN EUROPE
CEFTA................... CENTRAL EUROPEAN FREE TRADE ASSOCAITION
CHPP..................... COMBINED HEAT AND POWER PLANT
CITA....................... CORPORATE INCOME TAX ACT
CITUB.................... CONFEDERATION OF INDEPENDENT TRADE UNIONS IN BULGARIA
CoM....................... COUNCIL OF MINISTERS
CRC....................... COMMUNICATIONS REGULATORY COMMISSION
EA.......................... EMPLOYMENT AGENCY
EA.......................... ENERGY ACT
EBRD..................... EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT
EC.......................... EUROPEAN COMMISSION
EDC....................... ELECTRICITY DISTRIBUTION COMPANY
EEA........................ ENERGY EFFICIENCY ACT
EMEPA.................. ENTERPRISE FOR MANAGEMENT OF ENVIRONMENTAL PROTECTION ACTIVITIES
EPA........................ ENTREPRENEURSHIP PROMOTION AGENCY
EPA........................ ENVIRONMENTAL PROTECTION ACT
EU.......................... EUROPEAN UNION
FA.......................... FIXED ASSETS
FDI......................... FOREIGN DIRECT INVESTMENTS
FIA......................... FOREIGN INVESTMENTS AGENCY
FR.......................... FISCAL RESERVE
FSC....................... FINANCIAL SUPERVISION COMMISSION
GDP....................... GROSS DOMESTIC PRODUCT
GMO...................... GENETICALLY MODIFIED ORGANISMS
GS......................... GOVERNMENT SECURITIES
GVA....................... GROSS VALUE ADDED
HPP....................... HYDRO POWER PLANT
IAPT....................... IMPLEMENTING AGENCY FOR PROMOTION OF TRADE
ICT......................... INFORMATION AND COMMUNICATION TECHNOLOGY
IMF........................ INTERNATIONAL MONETARY FUND
LTD........................ LIMITED LIABILITY COMPANY
MAF....................... MINISTRY OF AGRICULTURE AND FORESTRY
MEER.................... MINISTRY OF ENERGY AND ENERGY RESOURCES
MFR....................... MOVEMENT FOR FREEDOMS AND RIGHTS
MLSP..................... MINISTRY OF LABOR AND SOCIAL POLICY
MNB....................... MARITIME NAVIGATION BULGARE
MoE....................... MINISTRY OF ECONOMY
MoF....................... MINISTRY OF FINANCE
MoH....................... MINISTRY OF HEALTH
MTC....................... MINISTRY OF TRANSPORT AND COMMUNICATIONS

ABBREVIATIONS USED

NA.......................... NATIONAL ASSEMBLY
NAMRB.................. NATIONAL ASSOCIATION OF MUNICIPALITIES IN THE REPUBLIC OF BULGARIA
NEC....................... NATIONAL ELECTRICITY COMPANY
NEDP..................... NATIONAL ECONOMIC DEVELOPMENT PLAN
NHIF...................... NATIONAL HEALTH INSURANCE FUND
NMSII..................... NATIONAL MOVEMENT SIMEON THE SECOND
NOPRD.................. NATIONAL OPERATIONAL PROGRAM FOR REGIONAL DEVELOPMENT
NPISH.................... NON-PROFIT INSTITUTIONS SERVICING HOUSEHOLDS
NPP....................... NUCLEAR POWER PLANT
NSI......................... NATIONAL STATISTICS INSTITUTE
NSSI...................... NATIONAL SOCIAL SECURITY INSTITUTE
OECD.................... ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT
OPEC.................... ORGANIZATION OF OIL EXPORTING COUNTRIES
OPF....................... OCCUPATIONAL PENSION FUND
PA.......................... PRIVATIZATION AGENCY
PIC......................... PENSION INSURANCE COMPANY
PIT......................... PERSONAL INCOME TAX
PPA........................ PUBLIC PROCUREMENT ACT
R & D..................... RESEARCH AND DEVELOPMENT
RB.......................... REPUBLICAN BUDGET
RDA....................... REGIONAL DEVELOPMENT ACT
RIEW..................... REGIONAL INSPECTORATE OF THE ENVIRONMENT AND WATER
SAC....................... SUPREME ADMINISTRATIVE COURT
SDR....................... SPECIAL DRAWING RIGHTS
SERC..................... STATE ENERGY REGULATORY COMMISSION
SHEI...................... STATE HIGHER EDUCATION INSTITUTION
SME....................... SMALL AND MEDIUM-SIZED ENTERPRISES
SSS....................... STATE SOCIAL SECURITY
UDB....................... UNION OF DENTISTS IN BULGARIA
UN......................... UNITED NATIONS
UNDP.................... UNITED NATIONS DEVELOPMENT PROGRAM
UPF....................... UNIVERSAL PENSION FUND
USAID.................... UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
VAT........................ VALUE ADDED TAX
VOC....................... VOLATILE ORGANIC COMPOUNDS
VPF........................ VOLUNTARY PENSION FUND

LIST OF FIGURES AND TABLES

The positive development of the Bulgarian economy continues in the first months of 2004. This is mainly expressed in the high GDP growth in the first quarter, low inflation rate, the condition of public finance, the growth of foreign investment and the active foreign trade turnover. Positive dynamics is also observed in the privatization, tourism and banking sectors, as well as in the capital market. The legislative and regulatory framework in the energy and transport sectors, in the high technologies and communications, as well as in the environmental and regional policies registers improvement as well. The upward trend in the value of the Estat index of business climate in Bulgaria also confirms the positive assessment of the economic development.

The current account balance, the condition of incomes and living standards, as well as the institutional and the financial aspects of the health reform remain problem areas of economic dynamics and economic policy. While progress has been registered in the enterprise policy, a number of pending issues remain.

In the first half of 2004 Bulgaria closed the last chapters of the negotiations for accession to the European Union, while commitments made, as well as Commission's financial framework for Bulgaria till 2013, which was announced in early 2004, will have key effect on the development of Bulgaria's economy in the next years.

An **economic growth** of 5.3 per cent against the same period of 2003 is registered in the first quarter of 2004. While industry accounts for the highest growth, its lead on services growth is negligible. Value added of industry registers a growth of 6.4 per cent on an annual basis (against 5.7 per cent for the first quarter of 2003). Growth in services is 6.2 per cent, catching up with industry and registering double values against the first quarter of 2003. Value added of the private sector (8.8. per cent) registers increase of 3 percentage points on the corresponding period of 2003. Investment in long-term assets (21.4 per cent against 11.6 per cent for the same period of 2003) registers sizable increase, reaching 18.7 per cent of GDP consumption (against 16.6 per cent for the same period of 2003). Final consumption (5.2 per cent) registers decline on an annual basis (5.9 per cent for the same period of 2003). Total domestic demand of the economic resource of goods and services preserves a higher growth against external demand. The share of the negative foreign trade balance of goods and services in GDP deteriorates by almost 4 percentage points (–13.3 per cent against –9.5 per cent for the same period of 2003). Still, import of investment goods registers higher growth against import of consumer goods, accounting for the difference in consumption and investment growth rates.

At the end of the first quarter of 2004 accumulated since year start **inflation** measured by consumer prices stands at 1.7 per cent against end of 2003 and is basically attributable to January price changes as a result of the new excise duties on tobacco products. Growth in commercial stock observed in recent quarters plus the deflation in March followed by a shallow consumer price dynamics in April and May (monthly inflation rates of 0.3 and 0 per cent accordingly), as well as the negligible rise of producer's prices of consumer goods, complete the assumption of saturated domestic consumer demand.

The quarterly **labor force survey** reveals some positive trends – the economically active population registers increase against the first quarter of 2003 (by 8.7 thousand people), employment has improved (by 79.5 thousand people), and unemployment has declined (by 70.8 thousand people). Productivity of labor has increased due to improved employment (by 2.9 per cent) and higher total economic growth (by 5.3 per cent). In the first quarter of 2004 **the unemployment rate** measured by the labor force survey stands at 13.3 per cent registering a decrease by 2.3 percentage points against the same period of 2003. Labor market processes are also confirmed by Employment Agency's data about **registered unemployment**, which has dropped down to 12.6 per cent in May, with the downward trend in unemployment continuing for a fifth month in a row.

The **current account** deficit deteriorated in the first quarter of 2004 as well (EUR 481.4 m or 2.5 per cent of GDP[1] against EUR 391.3 m or 2.2 per cent of GDP for the same period of 2003). The current account deteriorated against the same period of 2003 and against previous quarters mostly due to the deteriorated negative trade balance. The financial account is positive and stands at EUR 431.7 m (against a positive financial account of EUR 168.8 m for the same period of 2003. Yet the foreign direct investment-to-current account ratio has deteriorated – in the first quarter of 2004 FDI cover 61.1 percent of the deficit against 66.5 per cent for the same period of 2003.

Foreign trade continues its sustained growth – higher in imports than in exports. The European orientation of trade increases, particularly after the accession of the new Member States. Bulgaria gets specialized in the export of consumer goods and low-processed goods where the trade balance is positive. Higher domestic industrial consumption and the inflow of foreign direct investments encourage higher import of raw material and investment goods and maintain the sizable negative trade balance. Given the upward trend in investments, this deficit is not expected to get conquered in the near future, but it cannot be viewed as a serious threat to the economy.

In April 2004 the **Estat index** integrated estimate registered its peak value since the start of surveys. The higher index value was largely based on the registered growth in the Investment Attitudes and Condition of the Company components. A stable upward trend in the share of the companies which follow long-

[1] With 2003 GDP of EUR 17 594 m (NSI's preliminary estimates) and 2004 GDP projected at EUR 19 400 m (Source: BNB).

term development strategies is observed, while the share of companies which do not have competitive advantages registers increase as well. A slight improvement of entrepreneurs' assessments of the third component – Condition of the Company, is observed as well. The approval of the business for Government's initiatives for support of entrepreneurship registers increase. A stable upward trend of the confidence in the banking system is observed. The positive changes in the attitudes towards the tax policy persist. The lack of confidence in the transparency of public procurement procedures gives the most serious grounds for concern.

The Amendments to the SME Act were passed in the first half of 2004 whereby the institutional changes **in support of entrepreneurship** contemplated for about a year now became a fact. Most important changes include amendments to the definition of SMEs, which is largely harmonized with the European definition; changes in the regional scope of the SME Agency which is merged with EAST into a new Agency for Encouragement of Entrepreneurship; and the development of the enterprise policy in terms of its formulation and implementation. MoE will be responsible for formulating the enterprise policy, while AEE will be in charge of its implementation.

The idea of active **government support for the implementation of big investment projects** in Bulgaria was also approved. It was laid down in the Investments Promotion Act promulgated in May and was even applied in the biggest green field project since 1989 – the glass factory of the Turkish company Sisecam with a value of about USD 160 m.

Having registered considerable delay in recent years, **the privatization process made a big step forward.** The privatization of BTC was successfully completed after a two-year dramatic procedure. While the complex nature of the transaction generates procedural uncertainties, the privatization of the subsidiaries of Bulgartabac Holding registered notable progress. A successful start of the big privatization in the energy sector is expected upon submission of the final offers for the electricity distribution companies. The process of privatization of minority stakes on the stock exchange also gained pace. Minority stakes of the state in 936 companies, 33 detached parts and another 96 companies with majority interest have been sold since the beginning of 2004.

The tendency of improving the **access to finance** of economic enterprises continues. The banking sector increases its credit exposure to SMEs through dozens of new credit lines. The financial framework for Bulgaria and Romania for the period from their accession to the EU till 2009 was announced in the first half of 2004, while absorption of funds is conditional upon improved quality of investment projects and enhanced government administration capacity.

Against these positive trends, some **weaknesses of the enterprise policy** are observed. The project "Guarantee fund for micro-lending" has been further delayed; the Act on the Promotion of Investments in SMEs, while important for developing the "new" economy practices in Bulgaria, was not passed. New restrictive measures for bank lending have been adopted, imposed by IMF. Significant violations have been established with respect to assigning of public procurement contracts. The problem of representation of industry organizations has been partially solved with the conducted census of their membership. But the more important aspect of representation – approving the criteria for the provision of public services by industry organizations, has not been realized yet. The start of the privatization of many big enterprises has been delayed again.

Overall, very good execution of the budget under the consolidated fiscal program is reported for the first four months of 2004. According to data from the Ministry of Finance as of 30 April 2004, **the surplus on the consolidated budget** stands at BGN 528.9 m, registering an increase against the corresponding period of 2003 (BGN 409.7 m.). As at end of April **revenues** and aid stand at BGN 5 097.6 m, or 35.4 per cent of the total annual amount planned in the consolidated budget program. **Expenditures** for the period amount to a total of BGN 4 568.7 m, or 31.1 per cent of the annual amount of expenditures under Budget 2004. Regarding the constituent budgets, the national budget and the budgets of the social security funds register more significant expenditures.

As at end of April 2004, **the fiscal reserve** registers increase by BGN 566.3 m against end of 2003 and stands at BGN 4 415.1 m, of which BGN 3 822.5 m in deposits in BNB and BGN 1 975.5 m in foreign exchange assets.

After Moody's, Japan Credit Rating Agency (JCRA) and Fitch Ratings revised their ratings in a positive direction in the second and third quarter of 2003, at the end of June 2004 **Standard & Poor's (S&P) raised to investment grade** Bulgaria's sovereign ratings in foreign exchange from BB+/B to BBB-/A3 and the sovereign ratings in local currency from BBB-/A3 to BBB/A3. The trend is stable. The investment class rating achieved allows for future debt financing of Bulgaria's public and private sector at a lower price. At the end of April 2004 total **government and government-guaranteed debt** amounts to BGN 17 332.8 m at BNB central exchange rates for the lev at 30 April 2004. Total debt registers a decrease of BGN 346.9 m against the same period of 2004 due to the US Dollar exchange rate to the Euro dynamics in the reviewed period and the repayment of interest and principals. Total debt registers increase by BGN 823 m against the last quarter of 2003. The registered debt increase is due to accounted exchange rate variations and to the higher share of the domestic debt. At comparable data, the **debt-to-GDP ratio** has dropped from 47.8 per cent at the end of December 2003 to 45.6 per cent at the end of April 2004. The relative share of the debt in GDP is a more significant indicator compared to the nominal debt amount, as it gives idea of the growth rate of government debt and of the achieved economic growth. Bulgaria's integration in the Economic and Monetary Union is conditional upon maintaining the debt-to-GDP ratio at levels below 60 per cent.

At the end of June the Bulgarian government announced that on 28 July 2004 it would **exercise its right to redeem before maturity discount Brady bonds with a face value of USD 679.3 m,** issued according to the 1994 London Club of Private Creditors Agreement. Redemption with funds from the fiscal reserve is reasonable as far as interest service costs of Brady bonds exceed the interest income on the funds in the fiscal reserve. The choice of prepaying exactly this kind of debt is justifiable in respect of the clause, whereby the interest payable on discount bonds shall increase when GDP growth reaches 25 per cent of the 1993 level, included in the creditors' agreement (the clause will become effective not later than 2005).

The first months of 2004 are characterized by continuing decrease in the number of registered unemployed and a large number of successfully implemented **employment** projects and programs. Government's labor market policy is focused on prevention with a view to inhibiting the increase in the number of long-term unemployed and the need of social assistance. To attain these goals, it will be very important to get the business involved in MLSP's programs and projects in partnership with local authorities and non-government organizations.

While employment registers improvement, **the incomes and living standards** of Bulgarians remain at low levels with no signs of noticeable improvement in a close perspective. The official statistics for the first months of 2004 shows a negative growth in the real monthly wage of the employed and continuing downward growth rates in the income per household member against the same period of 2003. Despite the stable macroeconomic environment and GDP growth in recent years, far from all Bulgarians feel improvement in their living standards. Many surveys reveal sizeable poverty niches concentrated in ethnic groups, rural regions and the unemployed. Per capita income of Bulgarians is low at 28 per cent of the EU average. Hence it is very important to successfully implement the National Plan for Curbing Poverty and Social Exclusion adopted by the Government in January 2004.

In the first months of 2004 the privatization and restructuring of enterprises and productions of national importance brought in higher dynamics and changes in **the government-trade unions-employers relationship.** Previous results indicate a reasonable and productive approach by all process actors, cooperative behavior of the trade unions, which results in the long run in mutually acceptable solutions achieved through the social dialogue mechanisms. An important focal point of industrial relations in the reviewed period is the need to establish **special labour courts in Bulgaria.**

In the first half of 2004 major **legislative changes in the social sphere** included passing of Act on Guaranteeing the Claims of Workers and Employees in the event of Insolvency of their Employer; amendments to the Act on the 2004 Budget of State Social Security; amendments to the Labor Code in relation to Bulgaria's commitment to fully align Bulgarian labor legislation with the *acquis* and the Europe Association Agreement.

The chaos in **health care** continues, with no visible signs of progress in the health reform or any idea of how to solve the problems. By June 2004 NHIF, BDU and UDB have not agreed yet on signing the 2004 **National Framework Agreement**. Nothing indicates that it will become a fact in the near future, which is a signal of serious opposition on the part of medical care providers to the health care reform implemented by the Executive. While Bulgarian hospitals are accumulating debts again, NHIF registers substantial increase of the funds paid to medical institutions on clinical paths. NAO's Audit Report on the 2003 financial management of NHIF's budget and property revealed schemes and mechanisms for "draining" the public institution.

MoH and NHIF representatives make a proposal for developing a **Health Insurance Code** to regulate the rights and obligations of the parties to the mandatory health insurance, the mandatory social health assistance and the supplementary health insurance. It is not envisaged to have the health insurance contribution increased from 6 to 9 per cent in 2005 as proposed by primary care doctors; funds for health care are expected to amount to not less than 4.3 per cent of GDP as in 2004, despite that trade unions insist on not less than 6 per cent of GDP.

Since the beginning of 2004 focal points of **environmental policy** include legislative alignment in the areas of: protection of human health against the harmful impact of noise, waste management and release of genetically modified organisms in the environment. Discussion continues on a number of issues related to the practical dimensions of the arrangements achieved by Bulgaria on the Environmental Chapter of the negotiations in the context of national priorities against the positions of the ten new EU Member States and in the context of the new Water Sector Management and Development Strategy till 2015.

The banking sector preserves a dominant role in the financial sector and financial intermediation. In the first months of 2004 the banking system generally continued to increase its assets, deposits and net current profit. While credit expansion continues practically without delay since the beginning of 2004, the condition of banks remains stable with excellent indicators of capital adequacy and liquidity and well-functioning banking supervision. The first effects on credit growth of Government's and supervision's restrictive measures implemented or announced for a year now, may well be felt in the next months. Comparing the amount of assets and the credit exposure of Bulgarian banks against other countries in transition reveals that despite the growth observed in recent years, Bulgaria is still trailing behind most Central and East European countries. On the other hand, the whole region is also still far from the levels of the developed market economies. This indicates a serious growth potential of the Bulgarian banking system, including through credit expansion, notwithstanding the continuing debates on the optimum pace of this expansion.

Some positive trends, which characterized the Bulgarian **capital market** throughout 2003, continued in the first months of 2004. Stock exchange trade remains active, while in the first months of 2004 turnover, market capitalization and the stock exchange index register significant growth on an annual basis. The SOFIX broke the level of 500 points to reach record high values. The volume of traded securities has registered significant decline on an annual basis. One should note, however, the lack of development or decline of many indicators against the end of 2003. In the first months of 2004 trade in compensatory instruments and investment vouchers intensified basically due to public tender privatizations. While stable positive trends are observed, the role of the capital market in Bulgaria's financial sector remains negligible – as at end of May 2004 total market capitalization of the Bulgarian Stock Exchange – Sofia AD stood at 7.3 per cent of GDP's updated forecast for 2004.

Enriching the regulatory framework with the new Energy Efficiency Act and developing and approving the regulations to the two sector-fundamental laws will have effect on the short-term processes in **the energy sector** and on its development in a long-term perspective. The privatization of EDCs reached its final phase due to the parallel implementation of structural and legislative reforms. The issues related to the decommissioning of units 3 and 4 of Kozloduy NPP and the construction of a second nuclear power plant generated significant interest in the public space. The idea to set up an Energy Consolidation Company may prove important for the future development of the sector.

Positive development of the regulatory framework was observed in the **transport sector** as well. Passing on second reading three key acts in the land, water and air transport areas created conditions for increasing the share of the private capital in the sector, which in turn is a precondition for improving the quality and efficiency of sector's activities. The success of the first bond issue of BDZ reveals that there are many alternative ways to meet the need of attracting funds in the state-participation sectors. BRS was the first big state company in the sector which went in private hands via the stock exchange.

The completed privatization of BTC was undoubtedly the top event in the high technologies and communications sector in the first half of 2004. After a series of scandals, 65 per cent of BTC were finally sold to Viva Ventures, plus the third GSM operator license. Mobiltel also changed its owners for EUR 1.2 b, which makes the sale the biggest transaction in the Bulgarian telecommunications sector. The first signals of real competition on the fixed voice services telecommunication market came from the telecommunications operators licensed last year. After a significant delay, the final Plan for Implementation of Bulgaria's Strategy on e-Government was published in March. While the plan is a mandatory step towards e-Government and can be given a generally positive assessment, its implementation is conditional on solving the activities financing problem.

The positive development in **tourism** continues. The number of foreign tourists who visited Bulgaria in the first five months of 2004 registered increase of 25.36 per cent against the same period of 2003. Tourists from the EU (the ten new Member States excluded) account for the highest growth – 46.16 per cent, whereby the EU is emerging as Bulgaria's most important international tourism market. Greece is ranked first in terms of the number of tourists; Great Britain, Germany, France and Sweden also register high levels, as well as Macedonia, Serbia and Montenegro. The number of tourists from Italy and Russia registers increase as well. Bulgarian nationals, who travelled abroad in the first five months of 2004, total 1.455 m people, registering an increase of 20.2 per cent against the same period of 2003. Turkey accounts for the highest number of visits, followed by Greece, Serbia and Montenegro, Germany and Macedonia. In the first three months of 2004, revenues from international tourism total EUR 199.8 m registering an increase of 28.8 per cent. For the same period Bulgarians' spending on trips abroad totals EUR 154.9 m, registering an increase of 26 per cent. Net revenues from tourism for the first quarter of 2004 total EUR 44.9 m. Growth in the number of foreign tourists in the summer season is projected at 6-7 per cent. Great Britain, Russia and the Scandinavian countries are expected to account for the highest growth in the number of tourists. Important tourism-related strategic documents have been presented in the first months of 2004 - National Strategy and Action Plan for development of Eco Tourism, Strategy for Development of Rural Tourism. Amendments to the Tourism Act were passed as well, with focus on the facilitated treatment of tour operators and tourist agents by registration instead of licensing. Categorization of beaches and ski-tracks has been introduced as well.

Closing the Agriculture Chapter and completing the negotiations with the EU are the most important events determining the progress of reform and the development of **agriculture.** The arrangements achieved on the basis of available statistics for the last two years can be assessed as favorable for Bulgaria. Funds – EUR 1.55 b for the period 2007-2009, allocated for direct payments, market support (including intervention and export subsidies) and support for the rural regions – represent the maximum allocation from EU's budget. Actual drawing, however, is fully dependable on the sector's capacity to utilize these funds. For the purposes of utilizing the funds, there is a need to set up and strengthen a clear structure of agricultural producers and of their industry organizations; to create the necessary integrated control system (for example on farm land use, plants, number of animals), and to have in place a well functioning paying agency to manage direct payments based on the integrated control system data.

A couple of important events in the area of **regional policy** deserve noting since the beginning of 2004 – The European Commission announced the financial framework for Bulgaria; the Regional Policy Chapter of the negotiations for Bulgaria's accession to the EU was closed and the Regional Development Act was passed. The European Commission decided to allocate for Bulgaria and Romania 6 per cent of the funds for regional policy and structural instruments for the period 2007–2013, or EUR 22 b. The financial framework for Bulgaria for the transitional period of three years (2007 – 2009) is set at EUR 4.245 b. The largest portion of this amount – EUR 2.3 b, will be allocated for structural policies and for improving the living standards. Bulgaria made a commitment to have the country divided into 6 planning regions and 28 administrative regions. This is regulated in the new Regional Development Act which specifies the regional planning mechanisms. Allocations from European funds will be based on this planning as well as on settlements' indicators and most acute problems. The six centers of the administrative planning regions are Burgas, Varna, Vidin, Russe, Plovdiv and Sofia. The secondary legislation to the new Regional Development Act needs to be passed. It should develop further the provisions of the act and regulate the requirements for development, coordination, control and information support of planning documents and for the activity of the implementing bodies.

Gross Domestic Product

NSI preliminary data show 5.3 per cent growth in GDP for the first quarter of 2004 compared to the same period in 2003. It is the first time since 1998 that such a high growth rate of GDP has been reported in the first quarter of the year when the economic activity is usually low. After the slowdown of 3.5 per cent in the fourth quarter of 2002 continued also in the first quarter of 2003, this is now the fourth successive quarter of accelerated overall economic growth (from 4.2, 4.4, 4.9 to 5.3 per cent - from the second quarter of 2003 to the first quarter of 2004, respectively).

The Bulgarian economy has generated 6 per cent more value added compared to the first quarter of 2003. Same as last year, the industrial sector has reported the highest economic growth among the three major sectors of the economy, though insignificantly ahead of the services sector. The value added in the industrial sector has grown by 6.4 per cent on a year-to-year basis (versus 5.7 per cent growth for the first quarter of 2003). The largest contributor to this growth is the manufacturing industry (8.4 per cent), followed by the mining and quarrying (7.1 per cent) and electricity and water supply – by 1.6 per cent. The construction sector continues its sustained growth (7 per cent). It should be noted, however, that the growth in the services sector (6.2 per cent) is not only coming closer to the growth rate in the industrial sector, but is also two times higher compared to the growth in the services sector for the first quarter of the last year. The fastest growth in the value added was achieved by the financial intermediary services (31.1 per cent), followed by telecommunications (14 per cent), trade (12.2 per cent) and transport (6.4 per cent). Unlike its last year's downward dynamics, the agricultural sector shows a growing trend in the fist quarter of 2004 (1.2 per cent).

The value added growth in the private sector for the first quarter of 2004 (8.8 per cent) exceeds by three percentage point the growth rate reported for the same period in 2003. This is primarily due to the real growth in the business activity of private producers. The share of the private sector in the economy for the first quarter of 2004 continues to grow, generating 72.4 per cent of its value added, or 62 per cent of GDP (71.4 and 61 per cent, respectively, for the same period in 2003).

The high growth of investments in fixed assets (21.4 per cent vs. 11.6 per cent for the same period in 2003) results in increase of their share in GDP (18.7 per cent vs. 16.6 per cent for the same period in 2003). The growth in final consumption (5.2 per cent) has decreased on a year-to-year basis (5.9 per cent for the same period in 2003) due to the sizeable slowdown in individual household consumption (4.9 per cent vs. 6.8 per cent for the same period in 2003) and the increase in collective consumption (6.9 per cent vs. decrease of 1.9 for the same period in 2003).

The faster growth of domestic vs. foreign demand of goods and services in the Bulgarian economy reported in 2003 has been sustained during 2004. According to the estimates of the NSI experts this is due to the faster growth of intermediate consumption of goods and services vs. exports. Furthermore, intermediate consumption has a faster pace of growth than gross output (11.1 and 8.2 per cent, respectively, for the first quarter of 2004), which is most probably the result of increased producers' costs in connection with the compliance with the European norms and regulations.

The share of the negative balance on foreign trade of goods and services in the GDP has deteriorated by nearly 4 percentage points (-13.3 per cent vs. –9.5 per cent for the same period in 2003). The scissors between the growth of export and import of goods and services is opening even wider – the growth of export for the first quarter of 2004 (8 vs. 13.2 per cent for the same period in 2003) is two times lower than the growth in import (17.7 vs. 13.8 per cent for the same period in 2003). The positive trend is that import of investment goods rises faster than consumer goods, which has an impact on the difference between the consumption and investment growth trends.

The assessment of the expected high rates of economic growth during 2004 may be adversely affected by the substantial increase in inventory, 1/3 of which are in the commercial network, and the falling growth rate in individual consumption. The share of inventory within the use of GDP has increased to 3.6 per cent vs. 0.5 per cent for the first quarter of last year. Additional indication for the fact that the overall economic growth is unlikely to be sustained or accelerated over the second quarter is the slowdown in industrial production output and trade sales revenues reported in April. The rise in oil prices is most likely to have negative impact on the economic growth in the second quarter of 2004.

Inflation

The cumulative consumer price inflation between December 2003 and the end of the first quarter of 2004 has reached 1.7 per cent – following the change in prices in January when the new excise duties for tobacco products (average increase in prices by 20.8 per cent) and fuels (the prices of gas and liquid heating fuels rose by 4.8 and 3.1 per cent, respectively, and of propane-butane gas - by 4.9 per cent) have entered into force. In February consumer prices report a very low growth (0.3 per cent), which is again due to the introduction of new excise duties. In March the lower prices of food and the market price formation of non-food goods lead to deflation.

Industrial producer's prices on the domestic market have increased by 0.71 per cent in January and fell by 0.81 per cent in February – their decrease preceded the consumer price deflation in March. The increase in producer's prices by 1.37 per cent during the month of March resulted mainly from the increased costs of energy products (2.62 per cent) and intermediate products (1.43 per cent); the producer's prices for non-durable consumer products rose insignificantly – 0.16 per cent.

The increase in trade inventory over the last quarters combined with the March deflation and the subsequent flat consumer price dynamics in April and May (0.3 and 0 per cent inflation rates, respectively), as well as the weak growth of consumer goods' producer's prices confirm the assumption of oversupplied domestic market. This assumption is also supported by the NSI business surveys as of the end of May, which show lack of inflationary expectations among the businesses engaged in industry, construction and trade.

Employment and unemployment

It is during the first quarter of 2004 that we have the opportunity to compare on a year-to-year basis the data from the statistical survey of the labor force, which since the beginning of 2003 has been conducted under a different surveillance period. The comparative analysis reveals positive trends.

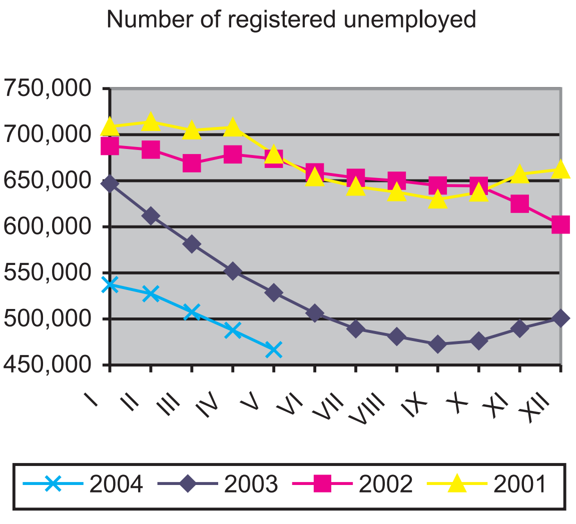
The number of economically active population rises (by 8.7 thousand) due to the increasing number of employed (by 79.5 thousand) and decreasing unemployment (by 70.8 thousand). It should be noted that rising employment by 2.9 per cent along with the faster overall economic growth (5.3 per cent) shows growing labor productivity over the first quarter of 2004 vs. the same period in 2003. Employment levels compared to the same period in 2003 have increased in the cities – by 1.3 per cent, and in the villages – by 1.0 per cent.

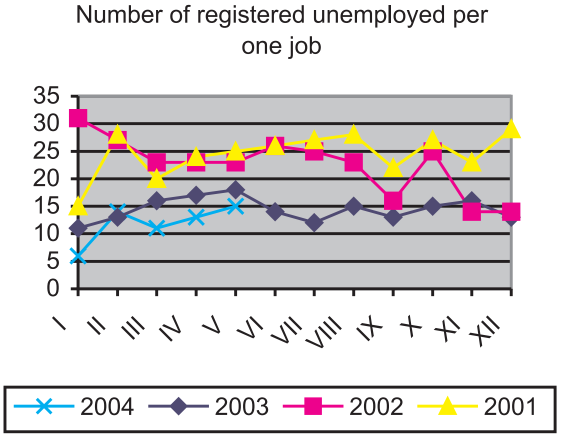
Unemployed numbered 428.8 thousand. Larger decrease in unemployment rates has been reported in the cities – by 2.6 per cent vs. 1.2 per cent in the villages. The relative share of permanently unemployed of total unemployed has decreased from 62.3 to 59.4 percent. Compared to the first quarter of 2003 the number of discouraged persons falls by 22.5 thousand, reaching 453.4 thousand in the first quarter of 2004. The unemployment rate for the first quarter measured in the survey of the labor force is 13.3 per cent, decreasing by 2.3 percentage points compared with the rate reported in the first quarter of 2003.

The processes in the labor market are also supported by the data on the registered unemployed with the Employment Agency. The employment rate in May falls down to 12.6 per cent. For a fifth month in a row there is a trend towards decrease of unemployment levels.

As of the end of May the registered unemployed numbered 466 717, or 62 001 less compared to the same period in 2003. The active demand for workers by private companies in the manufacturing industry continues its positive trend (4 352 announced jobs by employers) and trade (3785), followed by tourism (1992), construction (1959), agriculture and forestry (1951).

Figure 1. Number of registered unemployed





Source: EA

Balance of Payments[2]

The current account deficit of the balance of payments continues to deteriorate in the first quarter of 2004 (EUR 481.4 m, or 2.5 per cent of GDP[3] vs. EUR 391.3 m, or 2.2 per cent of GDP for the same period in 2003).

The largest contributor to the deteriorating current account compared to the same period in 2003, as well as to the previous quarters, is the negative trade balance. During the first quarter the trade balance stands at EUR 509 m (2.6 per cent of GDP), which shows deterioration by EUR 217.5 m compared

[2] According to BNB data as of 31 May 2004

[3] 2003 GDP stood at EUR 17 594 m (preliminary NSI data) and 2004 GDP projections – EUR 19 400 m (Source: BNB).

to the same period in 2003 (negative in the amount of EUR 291.5 m, or 1.7 per cent of GDP). The adverse impact on the foreign trade balance has been mitigated by the changes in the balance of current transfers for the reporting period (EUR 55.8 m, or –61.9 per cent) and in the balance on income (EUR 51.1 m, -56.7 per cent).

During the first quarter the export (FOB) stands at EUR 1718 m, or 5.2 per cent increase compared to the same period in 2003 (EUR 84.9 m), while the import (FOB) stands at EUR 2227 m, or increasing by 15.7 per cent (EUR 302.3 m). The import surpasses export by 32.5 per cent compared to 17.9 per cent for the same period in 2003.

The balance on services is negative and stands at EUR 37.5 m (0.2 per cent of GDP) but shows an improvement by EUR 20.4 m compared to the same period in 2003 (negative at the amount of 0.3 per cent of GDP). The balance on expenditures for transport services is negative (EUR -84.1 m vs. EUR –55.9 m for the same period in 2003), the balance on tourism is positive (EUR 44.9 m, or 0.2 per cent of GDP vs. EUR 32.1 m, or 0.2 per cent of GDP for the same period in 2003). Revenues from tourism stand at EUR 199.8 m, EUR 44.7 m (28.8 per cent) increase over the same period in 2003 (EUR 155.1 m), which is due to the larger number of foreign tourists visiting the country.

The balance on income (net) is negative, though slightly improving (EUR 118 m, or 0.6 per cent of GDP vs. EUR –169.1 m, or 1 per cent of GDP for the same period in 2003). Interest payments on securities issued by the government account for the largest share in the paid and outstanding income (EUR 185.2 m).

The net proceeds from current transfers in the first quarter of 2004 were higher compared to the same period in 2003 (EUR 182.8 m, or 0.9 per cent of GDP vs. EUR 127 m, or 0.7 per cent of GDP for the same period in 2003). Incoming transfers into the country stand at EUR 212.5 m vs. EUR 158 m for the same period in 2003. The transfers by private individuals account for the largest part of incoming transfers (EUR 162.6 m vs. EUR 118.4 m for the same period in 2003).

The financial account is positive and stands at EUR 431.7 m vs. EUR 168.8 m for the same period in 2003. The preliminary data show foreign direct investments inflows at the amount of EUR 294.1 m (1.5 per cent of GDP), or by 13% more compared with the same period in 2003. However the ratio between foreign direct investments and current account deficit is deteriorating – in the last quarter foreign direct investments cover 61.1 per cent of the current account deficit vs. 66.5 per cent for the same period in 2003.

Portfolio investments of residents abroad are increasing (by EUR 34.9 m) vs. decrease of EUR 3.6 m for the same period in 2003. Commercial banks have increased their portfolio investments abroad by EUR 31.3 m vs. EUR 16.9 m for the same period in 2003. Portfolio investments – liabilities decreased by EUR 65.9 m vs. decrease by EUR 61.1 m for the same period in 2003.

The balance on other investments – assets have increased by EUR 39.9 m vs. the increase of EUR 37.2 m for the same period in 2003. The foreign currency deposits of commercial banks aboard have increased by EUR 38.7 m, the deposits of non-banking enterprises abroad have also increased – by EUR 8.2 m.

The balance on other investments – liabilities have increased by EUR 291.9 m vs. an increase of EUR 5.8 m for the same period in 2003. Non-residents' deposits in commercial banks increased by EUR 76.2 m vs. a decrease by EUR 1.1 m in January-March 2003. During the first quarter the net loans disbursed to the non-financial sector stand at EUR 179.7 m, and to commercial banks – EUR 40.1 m.

The overall balance on the analytical presentation of the country's balance of payments for the first quarter of 2004 is negative and stands at EUR 28.5 m vs. EUR 164.3 m negative balance for the same period in 2003.

Foreign trade

The trade balance deficit has continued to show alarming trends of development. It is only for the first three months of 2004 that the volume of the negative trade balance (export FOB – import CIF) reached EUR 693.9 m, or 54 per cent increase over the same period in 2003. After a certain catch up between the growth rates in exports and imports at the end of 2003, now we are witnessing a surpassing growth rate in imports (15.8 per cent) compared to exports (5.2 per cent). The economic rehabilitation of EU is expected to stimulate exports, while the ongoing restructuring of the economy and the inflow of foreign direct investments trigger the growth in imports. For the time being the trade deficit is not seen as a major economic issue because it is subject to management and financing.

The different growth rates in **exports** by various classes of goods have changed the **structure of goods** compared to the first quarter of 2003. The 13 per cent decrease in the export of energy resources shrank their share in the total exports from 8.5 to 7 per cent. The share of consumer goods is increasing (from 35 to 36.8 per cent) as a result of the twofold growth rates. Raw materials sustain their share (over 42 per cent), while investment goods lose their positions due to the insignificant increase in the export volumes. Export of food reported the highest growth, which is indicative of the gradual revival of the food and beverages industry. The export of clothes and shoes represented 2/3 of consumer goods and together with food and furniture reach 85 per cent. Metals (ferrous and non-ferrous) represented almost half of the exported raw materials, registering 23-24 per cent increase due to the still high prices on the international market.

The geographic structure of exports verifies the already registered trend towards increasing the share of exports to EU – from 55.7 per cent over the first quarter of 2003 to 58.6 per cent in January 2004. The first three countries – Italy, Germany and Greece hold 63 per cent of the export to EU and Greece has already taken over Germany and reached 2nd place. The highest growth in exports is reported in the countries of CEFTA, whose share has increased to 7.2 per cent from 5.6 per cent in the previous year. Over half of the export to CEFTA was directed to Romania. The export to the Balkan countries is increasing, the major markets being Serbia and Montenegro, and Macedonia. The exports to Serbia and Montenegro have almost doubled compared to the first quarter of 2003. Though still at fourth place, Turkey has began to fall behind the first three countries due to the decrease in export volumes for this country in real terms.

The trend towards uniform acceleration of the imports by major classes of goods – consumer goods, raw materials and investment goods - continues (by 23-24 per cent over 2003) while imports of energy resources decrease further more. Thus, the import of goods for industrial consumption in the country reaches 68 per cent. Largest is the growth in imports of raw materials used in the food industry, esp. with respect to the large import of wheat and flour. Half of the imported investment goods were machinery, equipment and instrumentation. The largest share among consumer goods belongs to pharmaceuticals and cosmetics, while the largest increase was witnessed in the import of motorcars.

The geographic structure of imports has sustained its characteristics – 47.3 per cent represented imports from EU, and close to 8.5 per cent – from CEFTA. As a result of the improved trade relations the imports from the Balkan countries (mainly Serbia and Montenegro, and Macedonia) show the fastest growth rate; however, the export volumes are still insignificant (hardly 1 per cent). The increased imports from Turkey result from the growing imports of duty-free flour. The main importers – Germany, Italy and Greece have sustained their importance and positions. Traditionally, Russia occupied second place among the importers and Turkey – fifth place.

Foreign Direct Investments[4]

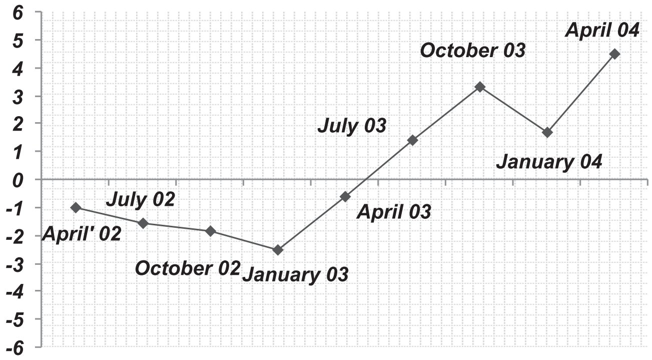
The inflow of foreign direct investments continues to grow. Preliminary data for the period January-March 2004 show 64 per cent growth over the same period in 2003. The reported volume of FDI amounting to EUR 425.1 m represents 2 per cent of GDP. Over 70 per cent of investments are intracompany loans extended from the direct investor to the investment enterprise and are indicative of the expanding production activity of the enterprises with foreign participation. The volume of received loans is probably much higher, because the greater part of the received short-term loans is already being repaid. The worldwide trends are to further move out the production operations from countries having higher production costs to those with lower production costs (the so called “outsourcing” process). With the accession of the countries from Central Europe into the EU and adjusting the production terms and conditions within the enlarged Union part of the investors are expected to redirect their business operations towards Bulgaria and Romania due to their improved business environment and still low costs. The observed investment dynamics set the grounds for higher expectations, i.e. the annual FDI volumes are expected to surpass the FDI of 2003.

4 According to BNB data as of 30 June 2004

The Estat index of business climate[5] in Bulgaria

In April the integrated value of the Estat index of business climate in Bulgaria rose as high as +4.51 (Figure 2) reaching the highest value ever since the survey was first conducted. Growth registered in the "Investment Attitudes" and "Condition of the company" components played a major role in pushing up the index overall value. This value is still in the neutral section of the scale. The economic environment for business development is still characterized as "neither favourable, nor unfavourable".

Figure 2. Dynamics of business climate condition



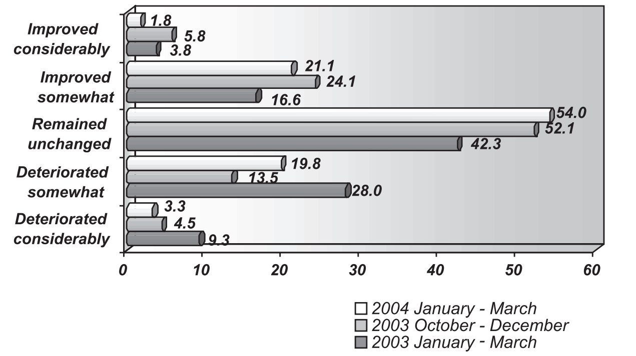
The survey reveals that managers can now much more distinctly identify the problems and barriers their enterprises face. The growing optimism, on the one hand, is accompanied by much greater requirements to the improvement of basic business environment components. On the other hand, entrepreneurs are increasingly critical of their businesses' condition, opportunities and perspectives.

General condition of the business sector

The value of Component I "Condition of the company" rose from 7.78 in January 2004 to 9.50 in April 2004.

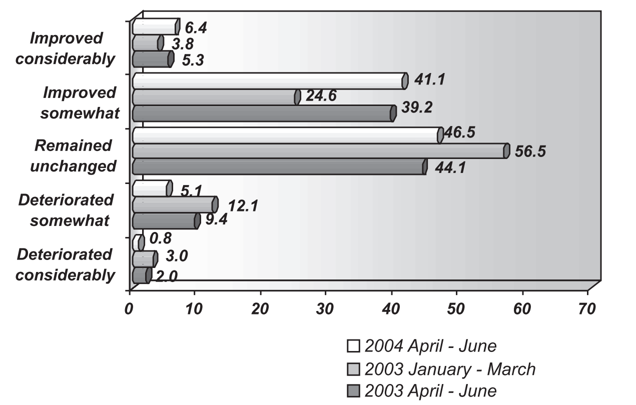
Survey results on the general condition of businesses reveal a very complex and seemingly paradoxical situation. According to 23 per cent of managers (Figure 3) their company's activity was improved during the last quarter. Just as big (23 per cent) is the share of those who responded that the condition of their business has worsened. The rate of scepticism is higher now as compared to the previous survey. The conclusion back then was that the assessment of the condition by economic players was subject to seasonal fluctuation. The comparative data analysis shows a certain decrease in the share of negative assessment and pessimism during the winter months of the year. For this reason at the beginning of the spring/summer period the assessment of the condition reaches its lowest values while activity and investment attitudes register their annual maximum.

Figure 3. In your opinion, has the condition of your business changed? (by quarters)



April registers a considerable growth in the number of managers who believe that the condition of their companies will be improving over the second quarter of the year (Figure 4). The share of 48 per cent is the highest in the survey's history. The presence of strong optimism is accompanied by a sharp decline in pessimism. Only 6 per cent of managers believe that the condition of their businesses will deteriorate.

Figure 4. Will the condition of your business change over the next three months?



The share of businesses with no competitive advantages continues its upward trend (Table 1). The key reason behind this is the lower assessment (as compared to the previous survey) given by managers to their own financial resources. It is worth pointing out that 8 per cent of respondents say their enterprises have no financial resources at all. The improved quality of computer technology and software, alongside information resources and Internet access, has favourable impact on the businesses' positions.

5 The survey was conducted in the period 8- 20 April 2004 among the managers of 398 companies and is representative at the "going concern" level. The sample criteria included the region, number of employees and type of ownership. The methodology behind the index and the mathematical model were developed by the Agency for Social and Marketing Surveys Estat.

Table 1. Companies position compared to competitors, %

Number of competitive advantages	2003			2004	
	April	July	October	January	April
none	27.1	28.5	30.8	31.6	34.3
1	16.6	16.0	17.1	15.3	16.4
2	22.1	17.9	16.4	19.3	15.1
3	11.6	10.8	11.6	15.3	11.5
4	9.5	11.5	11.6	8.3	13.6
5	6.0	7.9	5.0	5.0	2.6
6	7.0	7.4	7.3	5.3	6.6

The lack or poor quality of resources which are crucial to business activity and the deteriorated positions as compared to competitors are in discordance with the strong optimism among managers. A probable explanation could perhaps be sought in the context of international policy and more specifically in Bulgaria's NATO membership. The next several surveys will reveal whether the increased optimism is a short-lived and event-driven phenomenon.

Assessment of investment attitudes

The "Investment Attitudes" component has risen from 29.20 in January 2004 to 34.00 in April and largely contributes to the rise of the integrated Estat index.

Managers are increasingly focusing their efforts on the development of their core business activity under conditions of growing competition and while taking into account the perspectives of Bulgaria's EU accession. Meanwhile the high propensity for investments in other activities is being preserved.

There is a sustainable trend in the growing number of businesses pursuing a long-term development strategy. The percentage of managers who bind their business with strategic partners is also increased. The striving to develop the core activity is associated with overall mobilisation of financial resources. This explains why the share of managers stating deficiency of financial resources remained high (Table 2).

Borrowing from banks is the natural and, for the time being, the only alternative to compensate for the shortage of working capital and investment financing. The share of enterprises that would borrow a credit to implement their investment strategy is growing. The strongly pronounced positive trend in the attitude toward the banking system, evolving since late 2002, continued. The study measures it through two indicators – indirect, aptitude to taking bank credit, and direct, an assessment based on stability and reliability characteristics. Figures reveal a growing confidence in the banking system and managers' perception of credit institutions as a serious opportunity for business expansion. The reasons for the evolving positive attitudes could be sought mainly in the pro-active lending behaviour of financial institutions, the increased number of credit facilities and the growing popularity of these services. In addition there is a certain fall in interest rates on credits, in line with the medium-term downward trend in interest rates in the developed countries.

Table 2. Investment attitudes and corporate strategies, %

	2003		2004	
	July	October	January	April
In my current activity I experience deficiency of financial resources	72.8	70.8	72.0	69.3
I have a business strategy updated regularly	73.5	75.5	76.4	78.4
If I do not have funds for investment in core activity I will do my best to ensure them	88.1	88.9	88.4	91.2
I would draw a bank credit in order to invest	59.1	62.1	61.5	65.3
It is easy to find the employees I need	50.4	51.2	43.8	44.3
I would introduce new technology if this would enhance the quality of my products, regardless of whether this would have an impact on my profit	82.4	81.2	77.7	80.9

In April again a large share of entrepreneurs (67 per cent) responded that the Bulgarian market is a high priority for their company's activity. There is a direct connection between the propensity to introduce new technologies in production (81 per cent of businesses) and the striving to improve the quality at all stages of the manufacturing process (97 per cent of businesses). Managers see a certain threat to the implementation of this strategy in the greater difficulty in finding qualified personnel. The share of managers who face such problems is 56 per cent. This is the highest registered value of the indicator since the study first started.

Assessment of the business environment

The value for this component of the integrated Estat index is changed from -24.99 in January 2004 to -22.25 in April 2004.

By and large, entrepreneurs' attitude to the government's legislative and economic policy continues to be negative (Table 3). Meanwhile a large group of indicators characterising the business environment have gone up in value. Support for the statement that the legal framework creates equal conditions for all entrepreneurs has started to climb but is still not high enough. A positive change is observed in the business community's attitude to tax policy. The share of managers who believe that tax rates force companies to conceal incomes has dropped by another 5 points as compared to the previous review period while 41 per cent of respondents continue to maintain that the patent tax is unbearably high. This could be explained by the amendments to the Corporate Income Tax Act adopted at the end of last year. The entrepreneurs' assessment reveals their belief that they could use the financial resources which were freed in this way to reinvest and modernise their businesses. This also explains the sharp upward movement to 21 per cent of the share of respondents who agree that the tax system creates equal conditions for all companies in the country – the highest value ever since the survey was first conducted.

The relatively high share of entrepreneurs who have responded that social and health insurance contributions are a major burden to businesses is maintained – 71.8 per cent.

Table 3. Business environment – taxation and legal framework (share of those who agree with the statements, %)

	2003		2004	
	July	October	January	April
The patent tax is unaffordable to companies	55.2	51.7	41.5	40.8
Tax rates force companies to conceal incomes	77.3	79.5	72.6	67.3
Profit tax is affordable to businesses	26.6	23.2	29.1	32.2
The tax system creates equal conditions for all companies in the country	15.8	13.7	12.7	20.6
Social and health insurance contributions are a major burden to businesses	72.7	69.8	72.5	71.8
The legal framework creates equal conditions for all players	13.9	14.4	14.9	18.9

Businessmen are still reserved in their attitude to administration and administrative procedures (Table 4). In spite of the registered decline for key discontent indicators, 73 per cent of managers continue to be of the opinion that the practical implementation of the regulatory framework is difficult. 80 per cent of respondents share the opinion that most businessmen would be ready to pay in order to avoid the administrative complications. The transparency of procedures under the Public Procurement Act continues to be a strong cause of concern for the business community - in April support for the statement that these tenders are transparent and fair fell below 7 per cent, the lowest value since the survey was first conducted.

There is growing approval in the business community of government initiatives in support of entrepreneurship – currently 13.5 per cent of managers agree with the statement that the government promotes business development. This is the second highest value registered over the past two years.

Table 4. Business environment – administration and government policy (share of those who agree with the statements, %)

	2003		2004	
	July	October	January	April
Most businessmen would pay additional money to avoid difficulties with the administration	82.9	84.2	77.5	80.1
The practical implementation of the legal framework is difficult	77.9	73.9	76.1	72.5
The banking system is stable and reliable	40.6	49.8	52.7	56.3
The government promotes business development	8.8	11.2	10.9	13.5
Procedures under the Public Procurement Act are transparent and fair	10.2	8.6	6.9	6.5

Trends

Some positive trends could be outlined **in the area of enterprise policy** in Bulgaria during the first half of the year:

- A number of projects promoting entrepreneurship and clusters have been launched.
- The Investments Promotion Act was adopted while the economy is in a continuous process of accumulating fresh foreign capital.
- The first licensed special investment purpose companies started business more than a year after the statutory framework regulating their operations has been established.
- A vast number of minority blocks of state-owned shares in already privatised companies were sold through the Stock Exchange.
- The BTC privatisation deal was closed and the privatisation of Bulgartabac Holding and EDCs was launched.
- Enterprises' access to alternative financing has improved.
- The Commission for Protection of Competition improved its methodology for determining the size of pecuniary sanctions and fines.
- During the reference period measures were undertaken for the facilitation and speeding up of border transition.

At the same time, a **number of weaknesses in the economic policy** in support of enterprises can be identified:

- The project to establish a Guarantee Fund for Micro-crediting was not launched.
- The adoption of a law settling risk investments in SME was delayed.
- The issue of branch associations' representation remains unresolved.
- A number of restrictive measures on lending through the banking system were introduced.
- The start of the privatisation of a number of large companies was postponed yet again.
- Significant violations in public procurement procedures have been reported.
- Major weaknesses in the absorption of funds under the ISPA and SAPARD pre-accession programs have also been reported.

Encouragement of entrepreneurship

The **Act on Amendments to the SME Act** which was approved on first reading in January raised a debate on the state's role in support of the SME sector. The Parliament delayed the adoption of the law which was intended to lay down the provisions for establishing an Entrepreneurship Promotion Agency with 28 regional offices operating on the principle of public-private partnership. As SME managers have more trust in private sector representatives consulting their businesses' development, providing them with services following the principle of public-private partnership was a rational move by policy-makers to improve the level of trust in institutions supporting the development of the SME sector in Bulgaria. The postponed adoption of the Act by the National Assembly, however, also delays a number of positive policy developments envisioned in it[6].

The Act was fully adopted in July. To a large extent it reaches a synchronization of the Bulgarian SME definition with the one used by the EU. Although the legislative body did not raise the financial thresholds as was initially expected, according to the articles adopted on second reading a "small enterprise" is one employing less than 50 people and having an annual turnover of less than BGN 5 m (13 m according to the rejected draft law) and fixed assets value not exceeding BGN 1 m (BGN 9 m balance sheet value of the assets according to the rejected draft law). "Medium-sized enterprises" will be those employing less than 250 people, annual turnover not exceeding BGN 15 m (BGN 78 m according to the rejected draft) and FTA value not exceeding BGN 8 m (BGN 52 m balance sheet value according to the rejected draft law). Financial thresholds which are lower than those envisaged in the draft law aim to shift the focus of government support from large enterprises (according to the former definition) to smaller businesses.

The Guarantee Fund for Micro-crediting, which was provided for under the rejected alternative Act on Amendments to the SME Act, was also not set up during the review period although several projects have already been drawn up. ASME's idea was for the Fund to be financed not through the state budget (as was the underlying concept of the rejected draft law) but by private institutions or foreign donors with the possible participation of the state which was to be gradually withdrawn. The latter formula seems more viable for at least two reasons: first, it could generate an increasing amount of funds by the increase of its capital from private participation and, second, it does not use up budget funds which could be more rationally and transparently channelled to other government investment projects generating better long-term growth opportunities.

The **Act on Encouragement of Investments in SMEs** was also not finally adopted during the review period. It lays down opportunities for risk investments in Bulgarian SMEs and could be interpreted as a positive step in the enterprise policy, which would facilitate SMEs' access to advanced production technologies. A laudable measure by the government is to set aside state budget funds to guarantee bonds issued by companies for risk investment, with the amount of guarantees not exceeding BGN 50 m per year. It should be noted that BGN 50 m was exactly the amount that was envisioned under the rejected Act on Amendments to the SME Act to establish a Guarantee Fund for Micro-crediting. It is worthy to note the fact

6 "The Bulgarian Economy in the Fourth Quarter of 2003", Center for Economic Development, March 2004.

that the transfer of these BGN 50 m from the budget would better be made precisely to risk investment companies because projects of high-tech companies with short credit history could thus be given a chance to receive alternative funding. Channelling resources in this way is justified because currently the banking system does not provide ample resources to fund risk projects, and the listing of shares on the Stock Exchange or the sale of debt is not a popular practice with the majority of joint-stock companies and limited liability companies employing less than 250 people - that is, the companies to which the measures under the new law are targeted. A further argument in favour of transferring such resources is the decision of the OPIC investment fund (Overseas Private Investment Corporation) to invest about USD 200 m in risk projects in Eastern Europe, including in Bulgarian companies' operations. The final adoption of the draft law is still pending.

In connection with the move to introduce certain good practices in public-private partnership in Bulgaria, to simplify some business start-up procedures and also in connection with the better protection of interests in certain economic sectors during the review period, **the issue of branch associations' representation was placed at the top of the agenda**. A number of industrial branches feature more than one association - a fact that impedes gaining benefits that stem from the better outreach and improved cooperation between their members. The adoption of a draft law on branch associations is expected to clear up such issues.

During the first half of the year the Ministry of Economy launched several other **projects to support entrepreneurship**, including:

- Establishing Competitive Start-Up Companies.
- Development of Bulgarian Eco-Tourism.
- Introduction of Cluster Approach and Establishment of a Pilot Cluster Model.

For the first time enterprise policy in Bulgaria has put **clusters** on its agenda - perhaps the most advanced method to support the economy's export potential. Although the government is not in a position to directly influence the clustering of companies in certain geographical areas, launching such projects will have positive impact on the way economic policy priorities are being formed and also on the export potential of Bulgarian economy. There are plans to support the network of associated productions in the chemical industry in the Devnya industrial zone, the energy companies around Maritsa Iztok CHPPs, textile companies in the region of Ruse and companies in the ICT at the national level. A **Cluster Development Strategy** is planned to be drafted. Such a strategy should be financially associated with changes in the institutional structure promoting small and medium-sized enterprises. It seems logical that the planned regional ASME offices should take on the role of "communication agents" in certain clusters of the economy[7] – through better training opportunities and joint activities with businesses and also by exercising joint influence on certain cluster-targeted policies. The state's enterprise policy still has certain untapped resources; these are mainly to be found stepping up co-operation with the business community at the regional level. The identification of clusters and mediation between the enterprises to promote their development seems to be one of the most appropriate methods of support.

Encouragement of investments

The first half of this year saw a number of positive changes to Bulgaria's investment environment. The **Investments Promotion Act** was adopted on second reading; it lays down the regulatory foundation of the state policy in the area of investments. The Act officially acknowledges the equality between Bulgarian and foreign investors and puts emphasis on the importance of investment projects. The Foreign Investment Agency has been transformed into a **Bulgarian Investment Agency** which will take over the servicing of each investment project worth over BGN 10 m. Another novel feature is the introduction of customized services for investors holding a "class certificate" issued by the Agency not only at the central but also at the regional and municipal level, and the time to provide a certain service has been cut by one third. Administrative relief and preferential treatment will only be applied for investments in a new or expansion of an existing production operation, which will generate jobs and will be effective for at least 3 years. Currently small investors will not be granted such preferential treatment, under the presumption that with the gradual strengthening of administrative capacity these, too, will be covered. Investment will be divided into three "classes" by their size, with the precise limits laid down in the Regulations to the Act.

The entering into force of that Act in early August will promote the direct contact of businesses with the administration, cut down on deadlines and time for administrative servicing and increase the accountability of local administrative bodies in organising the investment process in the country. What is needed for the successful enforcement of the new Act is an urgent amendment to the State Aid Act and its Regulations to achieve full compliance with the acquis. It should also be noted that certain investment incentives provided for under the law may have to be dropped following the country's EU accession.

In parallel with the adoption of the new Act, the Council for Economic Growth has entrusted a working group of government and non-governmental experts to draft an **Investment Promotion Strategy**. The purpose is to lay down the guidelines and identify specific measures to improve the

[7] Rosenfeld, S. Advancing the Understanding of Clusters and their Opportunities for Less Favored Regions, Less Advantaged Populations, and Small and Mid-Sized Enterprises, p. 7, http://www.workforcepartners.org/upload/advan-understanding-of-clusters.pdf

environment and establish the appropriate conditions to attract more investments.

Proposals were put forth during the review period for the adoption also of an **Economic Development Act** aiming to lay down the priorities and measures of economic policy in the long-term aspect. The very title of the law attracts one's attention as it reveals the underlying intention for strong regulatory intervention by the state in business activities - which will hardly have favourable impact on economic development. The idea which has not even matured into a draft law yet, should perhaps include a framework for the drafting of national and regional economic development plans, coordination of economic policy measures with these in other areas of governance and the methods by which resources will be allocated to certain priority economic sectors or activities by the state to promote the competitiveness of Bulgarian companies.

The upward investment trend in the economy has persisted for the first half of the year. The Foreign Investment Agency projects about USD 2 b in foreign investment in the economy for 2004. Taking into account the potential proceeds from the privatisation of Bulgartabac factories, BTC and EDCs, the stated intentions for "green" field investments by a number of foreign companies, the continuing expansion of activity and reinvestment of profits by foreign investors, the growing investor interest in the Eastern Balkans as accession countries as well as the raised Bulgaria's investment rating by a well-respected rating agency gives us grounds to claim that such estimates are underestimated. Just a short list of some projects whose implementation is planned to begin in 2004 have been declared by business agents such as:

- Sisecam - glass factories - USD 160 m;
- Chelopech Mining - exploration and mining of ores and mineral deposits - USD 90 m;
- Mall of Sofia – shopping, entertainment and business center - EUR 50 m;
- Finvetro S.p.A. Group - manufacturing of car lighting glassware - EUR 20 m;
- Royal Frans Maas Group - logistics and shipment terminal – EUR15 m;
- Tyras - dairy products – EUR 10 m;
- Andromeda Real - business center – EUR 10 m.

Attitudes as regards the stepping-up of investment by Bulgarian companies are also improved and that is clearly seen by the significant growth of the "Investment attitudes" and "Condition of the company" components of the Estat index of business climate in Bulgaria.

The first **special investment purpose companies**[8] intending to invest, among others, in Bulgaria's fast growing real estate sector, have been licensed and are already active on the market. Incentives include tax relief (they are practically exempt from profit tax; however, 15 per cent of the distributed dividend is paid in the form of taxes by company shareholders). Expectations are that these companies will increase the securitisation of economy and will have positive impact on the development of the Stock Exchange. It is possible for them to take over part of the untapped resources of pension funds which have continued their growth during the review period. Thus pension funds are provided with an alternative investment opportunity in the Bulgarian economy.

Privatisation

Bulgaria's progress in the area of structural reforms and the privatisation of structurally significant state-owned companies are all factors crucial for the appraisal the country is given by international institutions and the investment community. The NMSII-MRF coalition has declared its intentions and determination to finalise the privatisation process a number of times over its three years in office and yet it was unable to register any progress on deals which are central to the development of market economy.

An assessment of the privatisation process in the period January – June 2004 would include the technical execution of the Privatisation Agency's Annual Operational Plan and a review of the state of the privatisation process in structurally significant companies.

Deals for the sale of 96[9] companies with the state as controlling shareholder and 33 detached parts[10] were concluded during the review period. This accounts for half of the privatisation deals planned for this year and therefore for the first time the PA is in a position to **report that its annual program is being implemented according to plan**. The sale of minority shares through the Stock Exchange also proved successful. For the period 1 January – 30 June 2004 shares from 936 companies have been transferred to private persons and companies[11].

The sale of stocks and shares of state-owned companies through the Stock Exchange employing various financial instruments is a method contributing to greater transparency and speediness in making the deals, getting a good price and reducing the large volume of unutilized compensatory instruments and investment vouchers. **In June, the Parliament extended the expiry dates of investment vouchers setting 30 June 2005 as the new expiry date**; formerly these would have been valid only by 30 June 2004. However, the option for the sale of majority shares by large state-owned companies such as Navigation Maritime Bulgare (NMB) and Bulgarian River Shipping (BRS) on the

8 Special Investment Purpose Companies Act (SIPCA), promulgated in Official Gazette, iss. 46, 20.05.2003. am. iss. 109, 16.12.2003. in force since 1.01.2004

9 Source: www.priv.government.bg

10 PA. Development of privatisation processes as at 30.06.2004. http://www.priv.government.bg

11 Same document.

Stock Exchange was not given green light. Thus in effect, and for political reasons again, the opportunity to make full use of the available compensatory instruments and investment vouchers was eliminated thereby hindering the development of the capital market.

Under the current Privatisation and Post-Privatisation Control Act, some state-owned companies are to be privatised following a special procedure - only upon the approval by the National Assembly of a strategy for their privatisation. This list includes not only BRS and NMB, but also the national air carrier Bulgaria Air, companies of the military industrial complex - VMZ – Sopot, Teraton, Kintex, the Electricity Distribution Companies, BTC etc. **BTC and the electricity distribution companies put aside, for the third year in a row now there has been no privatisation strategy drafted for either of these companies and their privatisation is being postponed.**

In May 2003 a Strategy for the privatisation of the seven EDCs was adopted; the companies were grouped into three pools. **Five companies were admitted to the final stage of the sale of the 67 per cent interest in electricity distribution companies**: EVN (Austria); PPC (Greece); Enel (Italy); CEZ (Czech Republic), and E.ON Energy (Germany). With the deadlines having been extended several times, final binding financial offers were expected to be filed by 9 July 2004. In view of the necessity to establish a common government policy for the privatisation of companies in the energy sector, the Economic Policy Council at its meeting in May 2004 adopted a decision thereby laying down tender procedures and competitions as the primary method for the sale of energy companies. This decision applies to 23 companies, including the three CHPPs Varna, Bobovdol and Ruse, for which a competition procedure for consultancy services was called.

The privatisation of companies in the Bulgartabac Holding AD system is currently underway. In late June 2004 Morgan Stanley, consultant for the deal, recommended in its report that some of the cigarette manufacturing companies should be grouped into pools before the privatisation procedure is launched. One of the packages includes Blagoevgrad BT and Slantse-Stara Zagora BT, while the other includes Sofia BT and Plovdiv BT. Companies in both pools will also get the brands for cigarette manufacturing. The holding's Managing and the Supervisory Board approved the consultant's report on the manner of privatisation of the companies. By the end of July 2004 a call for expression of interest will be made to investors along with the eligibility criteria for participation in the bidding procedures. Expectations are that the sale of companies in the pools will be complete by end 2004. The Bulgartabac Holding management will also launch a procedure of restructuring the subsidiaries of the holding itself. Companies attracting no investor interest will be closed down while cigarette producing factories in Vidin, Pleven, Haskovo, Assenovgrad and Shumen will be transformed into tobacco-processing companies.

In order to ease the social tension resulting from the restructuring of the holding and its subsidiaries, the government signed an agreement with the trade unions for the establishment of a Social Fund. The Fund will be financed with resources from the privatisation, international programs and donors. This Fund's resources are intended to cover unpaid wages, re-qualification of employees and lay-off compensations.

The privatisation is in full compliance with the Strategy for privatisation of companies in the holding adopted by the National Assembly in December 2003. The strategy lays down the government's high degree of responsibility and direct involvement in the process. The government agrees that the objectives of Bulgartabac Holding AD will be best achieved through the autonomous sale of each of its subsidiaries.

In essence, the Strategy envisages several stages of restructuring and sale of company assets. The first stage involves the incorporation of separate companies as autonomous economic units through transfer by the Holding of trademarks and licenses for cigarette manufacturing and settling of any legal and financial relations with the holding and the remaining subsidiaries.

The second stage involves the sale of those companies that investors find attractive and making decisions on how to dispose of the remaining assets of the holding. There are plans for some of the companies, including those abroad, to be closed down while others are to be rehabilitated.

The third stage involves the privatisation of an additional package of the holding's capital, while preserving state-owned stakes for the purposes of control over the management, conducting policies in the sector and meeting commitments made to buyers during the sale of the companies.

The Strategy aims to settle the disposal with the holding's assets within the current legislation framework – the Commercial Code and the Act on the Public Offering of Securities. The restructuring and privatisation of the holding will not be conducted as per the Privatisation and Post-Privatisation Control Act and the Privatisation Agency will not be involved in the process.

The existing structure and form of ownership in the holding and its subsidiaries is rather complex. Private investors own about 20 per cent of the holding's capital. The majority shareholder in the companies belonging to the holding's structure is Bulgartabac Holding AD. The state indirectly participates in the ownership of the holding's subsidiaries. Therefore **in implementing the Strategy the rights of minority shareholders should also be borne in mind - both as regards the holding and its subsidiaries**.

The deal for the sale of 65 per cent of the state-owned telecommunications company BTC was closed on 11 June

2004. The buyer is Viva Ventures, a subsidiary of the American Advent International investment fund. The price of the deal was EUR 280 m, including EUR 50 m in increase of capital. The investment program is worth EUR 700 m over a 5-year period, to which a further EUR 45 m for a social program and EUR 70 m for reinvestment of state guarantees will be added. As part of the privatisation scheme BTC paid the amount of BGN 54.160 m to be granted a GSM operator license. Within six months 20 per cent of the company's capital is expected to be offered on the Stock Exchange against compensatory instruments. This privatisation procedure started in 2002 and the privatisation agreement was signed on 20th February 2004.

Legal disputes surrounding the deal will continue even after its finalization. The Supreme Administrative Prosecution Office protested before the Supreme Administrative Court the decision of the Commission for Protection of Competition for concentration of commercial activity between BTC and Viva Ventures. The Supreme Administrative Court has initiated a lawsuit to settle the matter.

Additionally, the CPC decision to issue a third GSM operator license was appealed by several stakeholders – a fact which could further complicate the legal aspect of issuing the license. By early July 2004 the Commission for the Protection of Competition should have pronounced itself on whether the issuance of a license without a tender procedure is state aid and whether it is admissible but later extended the deadline citing its will to come to a more precise decision. The anti-trust institution has not yet received the European Commission's opinion on the issue. If the court's decision is that this is a case of inadmissible state aid, BTC will have to pay an additional sum to obtain the license.

At the end of 2003 the Minister of Economy initiated changes to the Privatisation and Post-Privatisation Control Act. The amendments were approved by the Council of Ministers and submitted for deliberation by the National Assembly on 10th May 2004. The main purpose of the amendments is to distribute the responsibilities in cases of privatisation of monopolies or companies of structural significance to the economy among the industry-related ministries as principals and the Privatisation Agency as the seller. The ministries' new responsibilities will include preparing the companies for privatisation and drawing up strategies for their sale.

Political responsibility for the privatisation process will be borne by the Council of Ministers while the powers of Parliament to adopt privatisation strategies will be abolished; all decisions for the sale of commercial companies with state interest and the approval of strategies for their sale will only be within the powers of the Council of Ministers.

Amendments to the Act also envisage a new structure for the two state agencies – the Privatisation Agency and the Post-Privatisation Control Agency. Supervisory boards, whose members were formerly elected by Parliament, will be eliminated. According to the draft law's authors, privatisation is part of the executive branch's economic policy and the Council of Ministers is the body conducting this policy.

The delayed restructuring and privatisation of companies in two sectors featuring the largest share of state interest – energy and transport - negatively influences the course of economic reforms in Bulgaria. The leasing under concession of Bulgarian roads, airports and ports is probably the best method to speed up the development of infrastructure which is currently among the poorest in Europe. In the months remaining until the end of its term in office, the government should focus its efforts on overcoming the delay in the area of privatisation and infrastructure concessions.

Access to financing

One of the major topics of debate during the review period were **the IMF-recommended restrictions on credit growth** aiming to avoid a further negative development of the balance of payments current account[12]. The credit growth rate is expected to slow down which will have negative impact on economic growth in general.

For the purpose of improving the functioning of the banking system, **the new credit register** was established covering all loans to households and businesses unlike the current practice which is to officially register only those not exceeding BGN 10 000. This step is expected to result in a more comprehensive picture of the actual debt rate of existing and potential clients of the banking system.

During the review period the opportunities to extend loans to SMEs grew in number; these were arranged by Bulgarian banks with foreign partners under various credit lines. **Some of the extended credit lines available for SMEs to be disbursed in 2004** include:

- UBB, Post Bank and Unionbank - a credit line for projects in the area of energy efficiency – EUR 50 m;
- EBRD – credit line for projects by Bulgarian SMEs of EUR 31 m, of these Post Bank and DSK Bank will absorb EUR 10 m each and Hebros Bank - EUR 6 m; Bulbank and TBI leasing companies will get EUR 2.5 m each;
- Raiffeisenbank - two credit lines of EUR 20 m and 10 m respectively for SMEs;
- ProCredit Bank - a credit line of EUR 10 m for SMEs;
- Hebros Bank – a credit line for agricultural producers worth USD 10 m;
- UBB – a credit line of EUR 10 m for financing projects in the area of agribusiness;

12 For further details please refer to Banking System Section.

- Unicredito (Bulbank) - a credit line for countries in the Balkan region – EUR 13.5 m, - of which 8 m for Bulgarian SMEs;
- Encouragement Bank – a credit line of EUR 5 m for working capital loans to be extended to Bulgarian export companies.

Under the JOBS project there are also plans to increase the financing of start-up companies by another BGN 3 m.

The Global Finance company and EBRD have set up a fund specially dedicated to investment in SMEs in Bulgaria and Romania (**Global Bulgaria and Romania Growth Fund**); financing from this fund is to be used to invest in stakes in start-up companies in the two countries. The initial capital is planned to amount to EUR 75 m, which will boost the development of alternative financing sources outside Bulgaria's banking system.

In June, the Council for Economic Growth adopted an Innovation Promotion Strategy according to which in 2005 loans will start to be extended under joint projects by businesses and research institutions. **A budget-financed National Innovations Fund will be established** to ensure the funding for these projects. Financing distributed by years is as follows: BGN 5 m in 2005, BGN 8 m in 2006, and BGN13 m in 2007. The mechanism for project assessment is not yet established; the Fund's Procedural Code is also not yet drafted.

The EU financial framework for Bulgaria for the period 2007–2009 was negotiated during the first half of the year. Bulgaria has the potential to double the indicative amount of EUR 4.245 b, 2.3 billion of which could be channelled to structural policies. During the abovementioned period Romania and Bulgaria will be able to invest in their economies the real amount of about EUR 9 b in total, with the amounts growing each year. In 2007, a total of EUR 1.648 b will be granted to the two countries, in 2008 the amount will be EUR 3.27 b and in 2009 it will reach EUR 4.13 b. **It should be noted that by the "Funds Per Capita" indicator Bulgaria gets the most favourable conditions in its financial framework as compared to all other new EU Mebmer States or candidate countries**. It was probably the expectation for these generous resources, together with the desire to adhere to IMF recommendations for fiscal discipline, which lead to yet another delay in the investment in large-scale infrastructure projects - notwithstanding the growing government resources in the fiscal reserve, the permanent budget surpluses and the funds allocated for investment in the economy outside the expenditure side of the budget. Preparations are under way for early repayment of debts to IMF with funds from the fiscal reserve - this could be classified as the most conservative possible answer to the economy's needs to boost economic growth.

Efficiently functioning markets

After the BTC deal was closed and the third GSM operator license was granted, the telecommunication services market in the country is expected to start functioning more efficiently from the consumers' point of view providing more affordable and better quality services as a result of the growing competition. Mobile operator prices in this country are still among the highest in Eastern Europe.

The Commission for the Protection of Competition has adopted a Methodology for determining the size of pecuniary sanctions and fines as per the Competition Protection Act. The new methodology was introduced on 1st June[13]. It underwent prior coordination with the European Commission which brings about a number of benefits regarding its implementation in future.

The methodology lays down three categories of infringements – minor infringements, serious and very serious infringements. This classification conforms with the approach adopted by the European Commission. The first category of infringements calls for financial penalties set between the minimum (BGN 5 000) and the average amount (BGN 150 000), for the second category the sanctions are foreseen to be in the amount close to the average amount of sanctions; while for the third category sanctions vary between the average and maximum amount provided for under the law (BGN 300 000).

During the review period **CPC continued levying sanctions and fines** for market conduct infringing fair competition. Multigroup and Overgas were fined BGN 40 000 each because of an agreement to avoid mutual competition in the construction of local gas-transmission networks; Alexandra Group was fined BGN 210 000 for abuse of its dominant market position; Nestle was fined BGN 300 000 – for a repeated violation of the CPA; for violations of the law in the management of advertising games Coca Cola was fined 100 thousand BGN, Zagorka - 215 BGN thousand, Vesoil-2002 - BGN 50 thousand; for unfair market competition – SIS Industries - BGN 60 000. During the review period the Commission for Protection of Competition also enforced other smaller fines.

In June the World Bank and EBRD published a report entitled **"Building Market Institutions in SE Europe"**, which says that "Bulgaria is one of the few countries in the region that have made significant progress competition protection policy since 1999"[14].

Preparation for the Single European Market

The utilization of financing from European funds prompted serious debate during the first six months of the year. It is

[13] Source: CPC. http://www.cpc.bg/news.php?type=0&id=132

[14] http://publications.worldbank.org/ecommerce/catalog/product?item_id=3512770

necessary to strengthen the capacity for the absorption of funds because the EU Financial framework negotiated for the period 2007–2009 would create favourable opportunities for the national economy only if a high absorption rate is achieved. Strengthening the capacity for funds absorption calls for further efforts in two aspects. The first aspect involves improving the quality of projects that apply for financing – essential here is the role of branch associations, of institutions supporting entrepreneurship, and entrepreneurs themselves and for this reason precisely addressing structural issues of enterprise policy and the issue of branch associations' representation is of highest priority. The second aspect is the active promotion of financing opportunities for SME projects through European funds (i.e. active as opposed to passive approach in identifying entrepreneurs with the appropriate capacity to utilize financial resources from pre-accession and structural funds) and improving the transparency in the administration's activities in this direction. The absorption of funds under EU programs is presented in the following table:

Table 5. Absorption of funds under pre-accession PHARE programs as of 31 May 2004

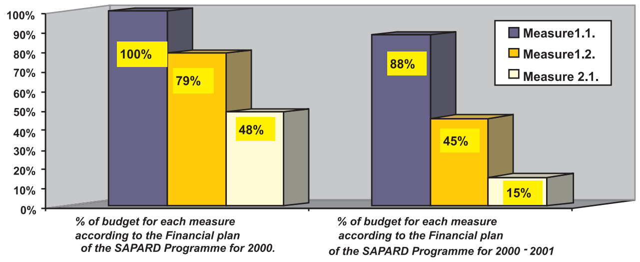
Program	PHARE '98	PHARE '99	PHARE 2000	PHARE 2001	PHARE 2002	PHARE 2003	PHARE 2004
Absorption (%)	94	86	78	55	44	18	n.a.

Source: Ministry of Finance

As can be seen from the table, the earlier a program was launched, the higher the rate of funds absorption, which is a normal process. The implementation of PHARE 2004 has not yet been started and some programs are currently being implemented which explains the lower share of absorbed funds. As a whole we could note that the absorption of funds under PHARE is satisfactory.

The absorption of funds for some measures under the SAPARD Program is satisfactory while for other measures the project implementation is being delayed which can be seen from the following figure[15]:

Figure 5. Funds absorption under the SAPARD Program for 2000 and for 2000 – 2001 for measures by 25.06.2004 for implemented projects



Highest absorption rate under Measure 1.1. "Investment in Agricultural Holdings", followed by measure 1.2. "Improvement of the processing and marketing of agricultural and fishery products" and Measure 2.1. "Forestry, afforestation of agricultural areas, investment in forest holdings, processing and marketing of forestry products". There are, however, measures for which not one single project has been completed[16] and it is with such measures precisely that problems concerning the quality of projects - and the administrative capacity we discussed earlier - are most easily identified.

Unlike other programs and measures for which the absorption of funds is satisfactory, problems surrounding the ISPA Program are most striking. The absorption of funds under this program, mainly intended for the development of infrastructure in the country is lowest – as few as 16 per cent[17]. Meanwhile infrastructure-related problems push down the rate of increase of our economy potential to generate long-term economic growth.

Among other problems related to our EU accession serious concerns were raised around the enforcement of the **Act on Health and Safety at Work** since 1 January 2004. Employers and trade unions represented at the national level and the Ministry of Labour however signed an agreement stipulating that in 2004 companies which do not fully meet the requirements, but have drafted an Action Plan, will not be closed down. This viable Action Plan needs to involve a risk assessment, a Contract with a Health and Safety Service and an intracompany group or committee on the working conditions which must be implemented by end 2004. Although quite substantial, investment in healthy and safe conditions at work would increase the competitive benefits in the long term and their implementation must be positively evaluated.

Complying with the requirements of the Single market is a challenge not only for Bulgarian companies but also for the state administration. In February **amendments to the Regional Development Act** resulted in the division of 6 planning regions. Although they have been established by Government Decree back in 1999, their institutionalisation results in new administrative obligations related to the absorption of structural EU funds because EU funds may only be utilized by administrative units servicing a population of between 800 000 and 3 000 000 people. The new planning regions are not administrative units but they allow for the utilisation of funds not to be hindered by statutory non-conformity with the EU's regional policy framework.

15 Source: MoAF. SAPARD Program as of 15.06.2004, http://www.mzgar.government.bg/Sapard/Napreduk.htm

16 For instance "Renovation and development of villages; protection and conservation of rural heritage and cultural traditions" and "Development and improvement of rural infrastructure" http://www.mzgar.government.bg/Sapard/news/Danni-za-komitet-30.06.2004.xls

17 Source: Ministry of Finance

Raising awareness of the Single market requirements related to the implementation of Bulgaria's Communication strategy for EU membership is also lagging behind. On the one hand, the Communication strategy is mostly directed to PR campaigns aiming to promote membership and suppress any possible euro-scepticism among citizens and businesses. It provides a budget of BGN 10 000 for each individual project aiming to make the business community familiar with the EU requirements for certain sectors. On the other hand, businesses need information on EU requirements by negotiation chapters, provided to them in a language that is easy to understand because most companies in Bulgaria still resort to legal and consultant's services only by matter of exception and to satisfy pressing needs, and not for making strategic decisions like the ones needed for preparation to enter the Single market. To date the Ministry of Economy[18], Ministry of Labour and Social Policy[19], MoRDPW[20], MoF, MoAF[21], Ministry of Justice[22], MoTC[23], MoH[24] and MEER[25] have published the European requirements to Bulgarian enterprises for some of the chapters of accession negotiations. A positive step during the review period **was the establishment of an Advisory Council under MoE** with the participation of business associations, aiming to make the business community aware of the commitments made during membership negotiations.

The delay of information about commitments made by the government in the course of negotiations creates a market for specialised advisory services in this area; the suppliers could be the non-government sector, branch and business organisations. For example the Bulgarian International Business Association has launched a project entitled **"Road Map for Bulgarian Economy Competitiveness"** aiming to boost the implementation of good manufacturing practices in Bulgarian enterprises in compliance with EU requirements. The project activities will mainly be targeted at the following areas – energy, telecommunications and information technologies, transport, agriculture, food-processing industry and environment. The Bulgarian Association of Food and Drink Industry (BAFDI, www.bafdi.com) also informs its members on requirements in this particular branch; the Bulgarian Industrial Association (www.bia-bg.com) also conducts a number of activities related to the popularization of requirements, arising from EU membership.

Trade policy

One of the major events for Bulgaria's business community in 2004 **was the accession of five CEFTA countries to the EU** and the impact this will have on trade flows. Because the Free Trade Agreement between countries from Central Europe fully complies with - and, to some extent, is a copy of, - the European Agreement, we have no reasons to believe that there will be any change in trade. Trade in industrial goods is completely duty-free and the fact of the accession will not change anything. As far as agricultural products are concerned, the new EU quotas on Bulgarian agricultural produce will take into account the new countries' accession. Only a limited number of export goods (processed agricultural products) on the EU market are levied with higher customs duty than in CEFTA, but Bulgaria's export of this type of goods is just a minor portion of the total.

The duty-free export to the EU without quantitative limitations for some foodstuffs has already been negotiated (chocolate, sugar, pasta products) which is expected to increase the export activity of Bulgarian producers. Because of the delayed adoption of the EU Regulation, the new trade arrangements are expected to become effective as late as 1 August while the initial deadline was 1 June. The most important issue still waiting to be addressed is related to wine exports – the CEFTA quotas used to be much higher than those in the EU and Bulgaria enjoyed relatively strong market position in these countries. It is a matter of negotiations to arrange the change of quotas. The customs duty for a number of vegetable varieties is expected to be dropped; these used to be traded under preferential terms on the markets of CEFTA countries and their production has already been adjusted to EU requirements. This will only become a fact after the signing of an Additional Protocol between Bulgaria and the EU, which is still being delayed.

Expectations are that by the end of this year the Protocol to the Europe Agreements on Conformity Assessment and Acceptance of Industrial Products will be signed. It will allow Bulgarian authorities in charge to assess the conformity of products while taking up less time and resources by businesses. Products assessed in this way will be allowed to freely circulate the market in Bulgaria and the EU and thus **the free movement of goods** in the single European market will become a fact.

In order to facilitate trade, **measures were undertaken during the reference period for the facilitation and speeding up of border transition**. Beginning early next year, the control and payments at border crossings will be made using the one-stop-shop concept which will increase two or three times the speed of cross-border traffic processing. The envisaged improvements of infrastructure at border crossings will allow for an accelerated traffic of goods across the border, it will cut down on transport costs and improve the efficiency of companies engaged in foreign trade activities.

Early this year discussions were held at the state level **regarding opportunities to overcome the growing trade deficit between**

18 http://www.mi.government.bg/integration/eu.html

19 http://www.mlsp.government.bg/bg/integration/euro/index.htm

20 http://www.mrrb.government.bg/page.php?P=191

21 http://www.mzgar.government.bg/EU/eu.htm

22 http://www.mjeli.government.bg/Eurointegration/Euroint.aspx

23 http://www.mtc.government.bg/EU_Integration/eurointegration.html

24 http://www.mh.government.bg/evrointegracia.php

25 http://www.doe.bg/cgi-bin/i.pl?l=1&p=588

Bulgaria and Russia and boost Bulgarian export. The issue of disproportional volume of trade is a long-standing one and has been causing concern not just in terms of the negative trade balance but also as regards exporters themselves. Apart from high duty rates they also face in the Russian market the lack of bank and insurance guarantees, unfair competition by off-shore companies, inadequate protection of intellectual property. Negotiations at the government level to bring down the duty imposed on certain sensitive goods are currently under way, but result could only be expected after the accession procedure for Russia to become a WTO member is started in 2005. WTO membership will force Russia to bring down the average import duty rates from the current 18 per cent to no more than 8 per cent. A positive aspect in bilateral relations is the agreement reached with the Russian state body in charge of certification and standardisation Gosstandart to open a Representative office in Sofia in order for Bulgarian exporters to be able to get the necessary certificates without delay. Such certificates will not only be issued for individual products but also for entire lines of products. The Bulgarian Hygiene Center is expected to be accredited by the relevant Russian authorities in charge of issuing certificates to Bulgarian exporters on foodstuffs and cosmetics.

The amendments to the Trademarks and Geographical Indications Act adopted earlier this year **aim to impose restrictions on the unauthorised import** and thus protect local manufacturers and importers from the unfavourable impact of smuggling and cut off access to the market for counterfeit items. All of this will eventually result in the normalisation of the market and boosting the advancement of real market relations.

Administrative and regulatory environment

There have been continuing efforts towards improving the general administrative and legal environment for establishing and operating a business in the country through **simplifying the regulatory regimes**.

Currently **changes are being made in the process of companies' registration aiming to speed it up**. Amendments are now being discussed to the Ordinance on Keeping and Safeguarding the Registers of Records. In addition, special forms for registration applications and entering into the records of changes of circumstances will be introduced. The amended Ordinance is expected to come into force from the beginning of 2005. A study into the capacity of the 28 district courts in the country will take place in order to establish a registration deadline. Expectations are that registration will be completed within seven days. Currently the registration of a company takes about 30 days. Establishing a deadline and a requirement for keeping it will be a guarantee of greater transparency and will result in lowering the corruption pressure on judges. In case he/she fails to keep the registration deadline, the judge will be subject to disciplinary sanctions. An option will also be provided to pursue a lawsuit on civil liability claims if damages were suffered because of the delay.

To facilitate citizens it is also planned for the Ordinance to contain a list of documents required for the registration of various types of companies. The court official accepting the registration request will be obliged to check if all required documents have been presented. According to current rules the official accepting the registration request is not obliged to make such a check and potential inaccuracies or missing documents may only be identified when the documents are submitted to the judge, which results in serious delays in the registration process.

A USAID-supported **project for reform in companies' registration** is currently under way. Agency experts presented their ideas in May, saying that for Bulgaria the best option was for the commercial register to be transferred to the Ministry of Justice and be united with the Register of Special Pledges. In addition, it is necessary to unite at the national level the tax, statistical, social insurance services and annual financial reporting. This approach will result in a substantial reduction of the time and expenses for registration, the doubling of effort and fees will be avoided; and also fraud and corruption opportunities will be prevented, eventually leading to the introduction of a single identification number for companies. USAID experts believe that introducing a single register would cost about EUR 3 m. These proposals are currently being discussed; representatives of the judiciary branch opposed the idea for the companies' register to be taken out of the court system citing that only magistrates are empowered to check if the entering into the records was done as required by law.

Regulation of public procurement

During the reference period **a National Audit Office report was published on the results of an audit of efficiency of the regime of control on public procurement** carried out by PIFCA under the Minister of Finance and the Public Procurement Directorate with the Council of Ministers[26]. The audit covers the period since the entering into force of the PPA in 1999 until 30 September 2003. Only for the period 01 January 2002 – 30 September 2003 PIFCA officials audited a total of 7 676 procedures. In 1 525 various violations were found. For 914 cases of public procurement no procedure was initiated at all. The most common violations include: absence of any procedure; failure to submit the data to the Public Procurement Register; case of discrediting the competitor by the contracting party; annexes concluded without legal grounds; conclusion of contracts before the appeal deadline; purposeful splitting up of the public procurement order to avoid the application of the law; conducting of procedures of direct negotiation without legal

[26] www.bulnao.government.bg/documents/Porachki.doc

grounds; difference between the provisions of the Contract and the proposal with which the applicant was approved.

The authors of this report conclude **that there is a lasting tendency of increase in the number of violations** of the PPA and the Ordinance on Public Procurement under the thresholds specified in Art. 7 of PPA.

The conclusions of this report and also a number of other analyses and studies once again demonstrate the pressing need to change on the legal framework regulating public procurement.

In March 2004 the Parliament approved on second reading the new **Public Procurement Act (PPA).** The Act complies with EU directives on public procurement for services, supplies, construction and the sectors of water supply, energy, transport and postal services. The essential purpose of the act was to ensure the efficiency in spending public funds. Procedures provided for under the law are based on the following principles: openness and transparency; free and fair competition; equality of all applicants.

This piece of legislation stipulates the types and subjects of public procurement; the thresholds above which a public procurement procedure is mandatory; the manner of defining the value of public procurement; the types of procedures; the rules for participation in procedures and the rules for public procurement; special rules for public procurement in the sectors of water supply, energy, transport and postal services; appeal and control procedures; establishment of a Public Procurement Agency and keeping a Public Procurement Register.

The new Act adopts higher thresholds for the various types of public procurement, without yet reaching EU levels. These are as follows:

Type of public procurement	*New threshold*	*Previous threshold*	*Threshold in EU*
	BGN.	BGN.	EUR
For services	90 000	30 000	130 000
For supplies	150 000	50 000	200 000
For construction	1 800 000	600 000	5 000 000

For the first time the terms and procedures for public procurement in biddings for projects where the threshold is above BGN 30 000 have been stipulated.

It is expected that raising the threshold will allow for limiting the number of flawed procedures and a more reasonable spending of financial resources for both contracting authorities and applicants, and also to constraining corruption. This however will only prove efficient if the public procurement procedures below those thresholds are fully transparent.

The Minister of Economy implements the government policy in the area of public procurement. The Act provides for the establishment of a **Public Procurement Agency reporting to the Minister of Economy**, which will assist him/her in implementing government policy in the area of public procurement. The primary powers of the Executive Director are as follows: to issue methodological guidance on the enforcement of the Act; to file legal claims on voiding public procurement contracts and voiding in case the law has been violated, approaching the competent authorities for exercising control on the law implementation; to keep the Public Procurement Register, to establish a Public Procurement Classifier; keeping the lists of contracting authorities and others.

In March 2004 the Council of Ministers adopted **the Regulation specifying the structure and the organisation of the Public Procurement Agency's activity**. The new administrative structure with the powers entrusted to it aims to overcome the problems related to the organisation and administrative capacity in conducting the government policy in the area of public procurement. Its establishment is expected to result in a stricter enforcement of the law and the unification of practices related to its implementation.

Keeping **a Public Procurement Register** is one of the Agency's most important functions. The current register contains incomplete or incorrect information on the procedures and contracts under the PPA. The Agency management's intentions are to enquire after and subsequently apply the best practices in this area by actively using modern information technologies, including by providing contracting authorities with the opportunity to fill in on-line the necessary data into the Register while complying to the E-document and E-signature Act. A Classifier of public procurement is currently under development; it will be based on codes applied in the EU (so-called CPV codes).

The new Act simplifies the process of appealing procedures as per the PPA – any applicant may file with the regional courts (and not with the Supreme Administrative Court, as the currently effective PPA provided) a claim requesting the repeal of decisions taken by the contracting authority.

Another major aspect in the Act is the **option provided for appealing the procedures before an arbitration court** provided the applicant has entered into an arbitration agreement with the contracting authority before submitting the offer. The competent arbitration authority under PPA will be an **Arbitration Court to the Public Procurement Agency,** which is to be established. This change will help facilitate and speed up the appeal procedures[27].

27 In 2003 there were a total of 10 000 public procurement procedures and almost half of these were challenged in court, which resulted in significant delay in conducting the procedures.

The arbitration procedure provides for several benefits: it is faster because this court will only have one level of authority, its decisions will be final and will not be subject to appeal before a higher court; arbitration procedure costs are lower; it enables specialised justice procedures by employing the services of competent persons and experts.

The new PPA provides for **preferential treatment of small and medium-sized enterprises** registered under the SME Act. These preferential treatments will be in force for the period 1 October 2004 – 1 January 2007. While assessing the offer submitted by a SME applicant, the price proposed by it will be considered to be the lowest, if it exceeds the price proposed by another applicant by no more than 15 per cent - for public procurement procedures in 2004; 10 per cent - for these, conducted in 2005, and 5 per cent for these, conducted in 2006. This scheme is planned to apply only when offers are submitted by applicants from countries which provide no equal access for Bulgarian companies to their public procurement and then only before 1 July 2007.

A major change in the Act is also the lowering of the maximum admissible amount of guarantee for a public procurement contract from 10 per cent to no more than 5 per cent of the public procurement value. The high rates for required guarantees for participation in procedures and execution of contracts were quoted by SME managers as one of the barriers to participation in such procedures.

The Act **preserves the option for public procurement to be carried out through commodity exchanges**, but the scope of contracts which could be concluded in this way has now been made smaller. A special list will be applied including only traditionally traded commodities which will be the subject of delivery under public procurement contracts. The list will be proposed by the State Commission for Commodity Exchanges and Markets subject to approval by the Council of Ministers in the Regulations to the Act.

For the first time Bulgarian legislation provides for the conclusion of compensatory (offset) agreements. These will be allowed for deals in the area of defence and security and will be regulated as part of a special Ordinance for public procurement in this area. With compensatory agreements the contractor undertakes before the contracting authority to make investments, execute procurement or construction agreements by Bulgarian companies, etc.

The new PPA shall enter into force on 1 October 2004. All implementing legislation must be adopted and promulgated by that date. These are: Regulations to PPA; Ordinance on public procurement under the thresholds, Ordinance on the terms and procedures of public procurement related to national defence and security; Public Procurement Classifier; Statutes and Organisation Regulations of the Arbitration court, and an Arbitration Procedure Tariff.

The prompt adoption of the above implementing legislation is of crucial importance for the enforcement of the PPA documents. For example with the three-fold increase of thresholds expectations are that under the new Ordinance the thresholds will remain 70-80 per cent of all Public procurement. It is especially important that document, apart from providing more flexible rules as compared to PPA, should also provide better transparency of procedures.

Some experts claim that the sharp (three-fold) increase will result in more corruption and create a prerequisite for more lawsuits to be filed to appeal the outcome of tenders. As a part of the discussions surrounding the new law, proposals were put forth to apply a more gradual increase of thresholds because a sharp increase could leave many public procurement procedures outside the Act's scope while the Ordinance of the Council of Ministers on public procurement below the thresholds could not guarantee sufficient transparency, openness and efficiency in spending budget funds.

The new Public Procurement Act is an important step towards EU membership because it is very important for the absorption of European funds and is one of the key instruments in this respect. The complete alignment of legislation in this area and the establishment of operational practices for its implementation would allow the country, when achieving full EU membership, to be prepared to effectively implement the complicated rules and procedures of the EU.

Corruption environment

In April 2004 Coalition 2000 presented its specialised survey on the scope of corruption practices carried out among entrepreneurs only. Worthy of mentioning is the fact that this survey finds the **lowest rate for the past two years of the indicator of "actually executed corruption deals"** in the country. The experts' opinion is that although it is quite early to make conclusions, figures reveal that the government's anti-corruption measures are gradually beginning to yield results. For almost all types of public services there is a trend of decreasing corruption pressure; this holds true above all for building permits and access to loans. The share of businesses which have paid unofficially sums of money to avoid a fine for a violation is continuing to grow. In Coalition 2000's latest survey there is an even clearer distinction between the two types of corruption – that initiated by civil servants and that initiated on the part of entrepreneurs themselves. We have enough data to claim that measures taken by the government have definitely influenced civil servants in a positive direction.

Another important conclusion to be made, apart from the lower number of corruption deals, **is the increase in the size of**

unofficial payments. For some services amounts of BGN 250 are still most common – including bribes one pays to be issued with a telephone number, work with companies' divisions (entering into the records) in the court, be connected to the electric grid, water supply.

The additional sums paid by entrepreneurs when being issued with building permits, authorisations, licensing, bank loans, court procedures when concluding a contract with large enterprises vary widely – from 250 to BGN 5 000. When applying for public procurement contracts 6 out of 10 companies say they paid over 1 000 BGN, while 20 per cent of respondents say they paid amounts of over 5 000 BGN.

Other sociological surveys **report similar results**. For instance, according to the monthly survey by Alpha Research public opinion polls conducted among businessmen for the period 20 March - 20 April, nearly 20 per cent of major public procurement contracts were granted following a bribe in the excess of 5 000 BGN.

Transparency International's latest report was published in March. Among 133 surveyed countries Bulgaria was ranked 54th according to the corruption index. Experts claim that the anti-corruption legislation in Central and Eastern European countries is superficial and features huge gaps in its implementation. The most serious problems were identified in the areas of political parties' financing, intercession and conflict of interests. The report says that political parties feature the highest degree of corruption in Bulgaria.

Reform in public administration

In April, the Council of Ministers adopted a **report on the condition of public administration** in 2003. According to that report the total number of public administration employees is 81 thousand people which accounts for below 4 per cent of all people employed. Public sector employees (including those in state education, health care and social welfare) account for 37.8 per cent of the total number of persons employed. This value is quite high for Bulgaria – by comparison in Belgium and Italy it is 23 per cent, in Portugal – 17.5 per cent, in Greece: – 12.9 per cent. The report said 1928 disciplinary sanctions were imposed on civil servants in 2003.

In April the results of a sociological survey on public administration were published. According to citizens who took part in the study, the grade mark for public administration is Good 4 /lowest 2, highest 6/. The study was conducted by the National Center for the Study of Public Opinion.

48 per cent of citizens believe that the unwillingness and incompetence of officials is behind slow or poor services. It should be noted however that 36 per cent of respondents consider the public administration performance to be improved.

The study found that nearly 75 per cent of citizens are not familiar with the appeal procedure when the provision of a given service was refused to them. This resulted in a decision that, starting next year, all institutions will be obliged to stipulate the appeal procedure, appeal deadlines and authorities in charge; this information will be printed on the application forms. In each institution a Customers Charter will be drafted by which customers will be kept informed on the requirements to officials providing various services, and the respective deadlines.

Over the coming months there will be a discussion on proposals by ministries for decentralisation and transfer of services to businesses. This will be done following certain rules and procedures which are to be drafted and adopted by the government. This measure is expected to result in the optimisation of the number of public administration staff.

In early June the Council of Ministers adopted **a Code of Conduct for public administration officials.** The Code stipulates that the official shall take actions, propose and make decisions leading to legal security, the elimination of arbitrary decisions and strengthening public confidence in government institutions. The Code is planned to also be applied by employees working under labour contracts. The adoption of such a Code of Ethics is necessitated by the crucial role of officials in public administration for conducting state policy and due to the higher requirements to civil servants as regards the discharge of their official duty. The principles which civil servants must adhere to in conducting their activity are as follows: legality, loyalty to society, responsibility and accountability.

The Code provides for a procedure to prevent a conflict of interests, stipulating that officials must not take part in the discussion, preparation, decision-making and implementation of such decisions, when they personally, or persons related to them, have interest in the respective decision or when they are in relationships with stakeholders which give reasonable grounds to doubt their impartiality. The Code regulates the rules of officials' servicing to citizens and colleagues, as well as their professional and personal behaviour.

Budget execution as of the end of April 2004

Consolidated budget (covers the national budget and all autonomous budgets – those of local governments, insurance funds, state universities, Bulgarian Academy of Science, Bulgarian National Radio, Bulgarian National Television, Supreme Judicial Council, as well as extra-budgetary funds and accounts on central and local level).

Overall, we witnessed a fair rate of execution of the consolidated fiscal program throughout the first four months of 2004, with some budget items showing positive performance as compared to the same period of last year. According to data provided by the Ministry of Finance as of 30 April 2004, **surplus on the consolidated fiscal program** has increased as compared to the corresponding period of 2003 (BGN 409.7 m) and currently amounts to BGN 528.9 m. At the end of 2003 a surplus of BGN 0.937 m was registered on the consolidated fiscal program. The trend is expected to persist over the next several months. Due to the anticipated revenue surplus on the consolidated fiscal program it is possible for the deficit in 2004 to be lower than the amount planned under the State Budget Act; another option is to use such surplus revenues to finance part of the conditional expenditures on infrastructure projects under the “Financing” item.

Revenues and aids at the end of April 2004 amount to BGN 5 097.6 m, or 35.4 per cent of the planned total annual amount in the consolidated program. By comparison, in the first four months of 2003 consolidated budget revenues equalled BGN 4 631.2 m or 34.2 per cent of the planned annual amount and 32.9 per cent of generated revenues. Tax revenues and indirect tax revenues in particular made a major contribution to good execution of the revenue part. **Expenditures** during the period amount to a total of BGN 4 568.7 m, or 31.1 per cent of the annual expenditures under Budget 2004. By comparison, during the same period of the preceding year expenditures amounted to BGN 4 221.5 m (31 per cent as compared to budget estimates and 30 per cent of expenditures made during the year). With regard to constituent budgets sizeable expenditures are reported in the national budget and the budgets of social insurance funds.

The trend of spending a substantial portion of the expenses budgeted in the consolidated fiscal program at the end of the year, which has been witnessed during the past several years, will probably persist over the course of next year. Past experience gives us ground to expect that the key expenditure items to be spent at the end of the year will include infrastructure projects financing, the financing of NHIF, unpaid amounts for municipal state-delegated activities, the Christmas supplements to pensions, and the “thirteenth” salary for employees of budget-financed institutions.

National budget (comprising the central budget, budgets of ministries and agencies and the budget of the Audit Office)

A **surplus** at the amount of BGN 405.3 m is reported in the national budget. Revenues amount to BGN 3 368.2 m. (37.2 per cent of all revenues planned for the year) while expenditures and transfers amount to BGN 2 963 m (31.9 per cent of the annual amount according to 2004 budget estimates). By comparison, last year these values were respectively BGN 2 878.1 m (37.6 per cent of planned and 34.1 per cent of reported revenues) and BGN 2 594.1 m in expenditures and transfers (32.3 per cent of the program and 30.3 per cent of the total amount of expenditures and transfers made during the year).

Central budget

The surplus under the central budget amounts to BGN 287.3 m with revenues amounting to BGN 2 895.2 m and expenditures and transfers to BGN 463.6 m and BGN 2 144.4 m, respectively.

Fiscal reserve (covers cash in BGN and foreign currency on all current and term deposits with the BNB and commercial banks of the central budget, the budget funds of ministries and agencies, the National Social Security Institute, the National Health Insurance Fund and their extra-budgetary accounts and funds, as well as other high- liquid low-risk financial assets in foreign currency of the government).

The fiscal reserve at the end of April 2004 increased by BGN 300.9 m as compared to the preceding month and amounts to BGN 4 415.1 m; of these resources deposits in BNB amount to BGN 3 822.5 m and funds in foreign currency assets amount to BGN 1 975.5 m. Table 6 shows the dynamics of the fiscal reserve over the reviewed period.

Table 6. Indicators of the fiscal reserve (FR) according to the Agreement with IMF (BGN m)

	As of 31 December 2003	As of 31 January 2004	As of 29 February 2004	As of 31 March 2004	As of 30 April 2004
Total amount of FR	3 848.8	3 726.5	3 687.9	4 114.2	4 415.1
FR funds in BNB deposits	3 280.1	3 138.4	3 146.7	3 503.2	3 822.5
FR funds in foreign currency assets	2 289.3	1 951.6	1 940.0	1 986.8	1 975.5

Source: MoF data

Municipal finance

As of 30 April 2003 municipal budgets reported a surplus of BGN 103.1 m with BGN 294.5 m in revenues, BGN 428.6 m in net transfers and BGN 620 m in expenditures.

Revenue side of the national budget

Tax revenues

Tax revenues to the national budget as of 30 April 2004 amount to BGN 2 677.5 m against BGN 2 188.1 m during the same period of last year. Tax revenues execution by the month of May 2004 is 35.8 per cent as compared to the annual revenues planned in the State Budget Act. As of the end of April 2003 the execution of tax revenues to the national budget was 35.9 per cent of the annual amount of revenues planned under the State Budget Act.

VAT accounts for the highest relative share of the **tax revenues**– 44.5 per cent of total tax revenues as compared to 46.9 per cent of the total, executed over the same period in 2003. Execution of VAT for the first four months of 2004 is BGN 1 192.7 m (35.7 per cent of planned VAT revenues for the entire year), against BGN 1 025.9 m at the end of April last year (34.9 per cent of the planned total annual amount). The key reason behind such increase is improved VAT revenues from imports as a result of imports growth during the first four months of 2004 as compared to the same period of last year.

Excise duties and charges on liquid fuels account for a high relative share of revenues – BGN 503.2 m or 18.8 per cent of total tax revenues. The tax execution as compared to annual estimates is 28.8 per cent as of the end of April against 28.3 per cent at the end of April 2003. New higher rates on liquid fuels and tobacco products influenced the growth of revenues from excise duties. The execution of revenues from excise duties on locally manufactured products is not as good, which is due to the smaller volume of fuel production. Another factor accounting for the size of revenues from excise duties are the prices of energy resources on international markets

The relative share of revenues from **corporate tax** by 30 April 2004 (BGN 414.1 m) is 15.5 per cent of tax revenues against 21 per cent for the preceding year (BGN 458.9 m). Its execution as compared to annual estimates is 48.7 per cent. There are two fundamental factors which contributed to the decrease of corporate tax revenues as compared to the first four months of last year. First, advance instalments during the review period were paid at a different tax rate (23.5 per cent in 2003 and 19.5 per cent in 2004) and a different amount of taxable profit. On the other hand, there is also the influence of non-payment of advance instalments by businesses which had overpaid taxes or reported a loss in 2003.

The share of revenues from **personal income tax (PIT)** by the end of April is 14.2 per cent of the tax revenues against 5.6 per cent for the same period of last year. The execution of PIT on a net basis is BGN 380.7 m or 34.3 per cent as compared to the annual estimate. For the same period last year collected revenues amounted to BGN 123.4 m or 32.9 per cent of annual estimates. The major reason for the substantial increase of PIT revenues as compared to the same period of last year was the minimum social insurance threshold introduced since 1 January 2003. Increased revenues are due to proceeds from the tax levied on income under labour contracts payable for 2003, and also due to the payment of tax liabilities under the annual tax return for non-labour relationship in January using a 5 per cent discount.

Revenues from **customs duties and charges** amount to BGN 90 m or 44 per cent against annual estimates. The increase as compared to the same period of 2003 amounts to BGN 21.1 m. The Customs Agency's 2003 financial results were published in January. Total revenues from VAT, excise duties and fines collected by the Customs Agency on the cash-basis execution of the 2003 national budget amount to BGN 3 200.3 m, an 112.8 per cent execution as compared to budget estimates. As compared to 2002, generated revenues in 2003 registered an increase by BGN 495.9 m, or 18.3 per cent.

Non-tax revenues and aids

Non-tax revenues to the national budget at the end of April amount to BGN 683 m or 43.6 per cent as compared to annual estimates. The amount remains unchanged as compared to last year. **The one-off annual instalment financed from the difference of BNB revenues less expenditures** in the amount of BGN 170.9 m (against a total annual estimate of BGN 156 m) contributed to the generated non-tax revenues. A fairly good execution is reported of **other non-tax revenues to the central budget** (76.2 per cent of annual estimates).

Taken as a whole, the trend of inaccurate budget revenue estimates persists, thus inhibiting the efficient planning of budget expenditures on annual and quarterly basis. The practice of spending the surplus generated in the course of the year during the last months of the year may lead to the sub-optimal utilization of available resources.

Expenditure side of the national budget

Expenditures

The highest relative share of 37.9 per cent of total expenditures belongs to **running costs** (BGN 744.3 m). These include costs for medicines, fuel and energy, hired services, current repair, as well as defense and security expenditures.

Interest paid on foreign and domestic debt servicing as of the end of April amounts to BGN 374.2 m of which BGN 62.2 m on domestic loans and BGN 312 m on foreign loans. The relative share of expenditures for interest payments during the period accounts for 12.6 per cent of the total budget expenditures (against 15.7 per cent in the first four months of 2003).

The trend of increased **subsidies** both in nominal terms and as a share of total expenditures has persisted - BGN 211.4 m or 41.7 per cent of annual estimates. By comparison subsidies granted by the beginning of May 2003 amounted to BGN 148.2 m or 28.4 per cent of the annual amount planned in the national budget. The dynamics of subsidies granted during the first four months of 2004 leads us to believe that the funds actually allocated in the course of the year will exceed budget estimates.

There is also an increase in **social and scholarship expenditures** by nearly 14 per cent as compared to the same period of last year - from BGN 198.2 m to BGN 225.5 m. The latter's share in the total expenditures remains relatively constant.

Transfers

Net transfers (the difference between received and allocated national budget transfers) from the national budget to other budgets amount to BGN 999.2 m. The national budget has allocated to municipalities BGN 426.3 m or 36.6 per cent of the planned total annual amount. Transfers made from the central budget to the budget of NSSI amount to BGN 323.2 m or 32.7 per cent of the annual estimates. The central budget subsidy to the budget of the judiciary amounts to BGN 53.2 m or 35 per cent of the annual amount.

Foreign and domestic debt

After Moody's, Japan Credit Rating Agency (JCRA) and Fitch Ratings revised in a positive direction their assessment during the second and third quarter of last year (Table 7), at the end of June 2004 **Standard & Poor's (S&P) upgraded** the foreign currency sovereign ratings of the Republic of Bulgaria **to an investment class** (BBB-/A3) and the local currency sovereign ratings from BBB-/A3 to BBB/A3. The rating prospects are stable. According to the agency Bulgaria's creditworthiness is supported by its great potential for economic growth, its prudent fiscal policy and its European orientation which will most likely result in EU membership in 2007. Bulgaria's relatively low development level and poor foreign liquidity are still holding back further rating upgrades. The stable prospects accompanying the credit rating reflect the balance between the strong performance of the fiscal policy and the poor foreign liquidity. Future credit rating upgrades will depend on maintaining a precautionary policy compatible with the Currency Board arrangements in Bulgaria, and also on successful EU accession. According to the agency, special attention should be paid to controlling the foreign-currency balance which, on Bulgaria's accession to the Economic and Monetary Union, will remain a weakness both for the economy and for Bulgaria's credit rating. Persisting omissions with regard to Bulgaria's stability and reform-oriented policies - for example a significant delay in the planned EU accession and later to the Economic and Monetary Union - could result in a pressure to downgrade the rating.

Table 7. Credit Rating as of 30 June 2004

Agency	Foreign currency			Local currency		
	Long term	Short term	Prospects	Long term	Short-term	Prospects
Fitch	BB+	B	Positive	BBB-	-	-
JCRA	BBB-	-	Stable	BBB	-	Stable
Moody's	Ba2*	-	Stable	Ba2	-	-
Standard & Poor's	BBB-	A3	Stable	BBB	A3	Stable

* The quoted Moody's rating applies to bonds and long-term securities in foreign currency. The rating for long-term bank deposits in foreign currency is Ba3.
Source: MoF data

At the end of April 2004 **the total amount on government and government-guaranteed debt** was BGN 17 332.8 m at BNB's central exchange rates for the Bulgarian lev as of 30 April 2004. As compared to the end of last year an increase in the total amount of debt is reported by BGN 823 m. The registered debt increase is due to the reported exchange rate fluctuations and the increased share of domestic debt. At comparable data the debt/GDP ratio has dropped from 47.8 per cent at the end of December 2003 to 45.6 per cent at the end of April 2004. As compared to the end of April 2003, the total amount of debt was reduced by BGN 346.9 m, due to the US dollar exchange rate dynamics against the Euro over the review period and the repayment of interest and principal.

In dollar terms, however, government and government-guaranteed debt has decreased by USD 73.8 m for the period from end-2003 to end-April 2004 (from USD 10 661.4 m to USD 10 587.6 m according to BNB central exchange rates for the respective dates). This is due to the fluctuations of the Euro exchange rate against the US dollar, and also due to the changed foreign currency structure of the debt. As of the end of December 2003 the dollar-denominated debt accounted for 44.9 per cent of the total amount of the government and government-guaranteed debt while at the end of April the dollar-denominated debt had reached 42.2 per cent. As a comparison, the share of Euro-denominated debt increased from 32.4 per cent of the total amount as of the end of December to 34.5 per cent as of the end of April 2004. (BGN debt also registered an increase in the debt structure – from 9 per cent at the end of December 2004 to 9.6 per cent at the end of April 2004).

Over the next months the amount of the debt will probably continue to be predetermined by the dynamics of the exchange rate of the Euro against the US dollar and the changes in the foreign currency structure of the debt. At any rate, however, the total debt/GDP ratio will be preserved within the Maastricht limits and will probably keep its trend of progressive decline.

Foreign debt

According to data from the Ministry of Finance, at the end of December the size of foreign debt rose to EUR 7 603.1 m (against EUR 7 356 m at the end of 2003), the government debt accounting for EUR 7 152.8 m (against EUR 6 903.1 m at the end of December) and government-guaranteed debt amounting to EUR 450.3 m (EUR 392.3 m as of 31 December 2003). In dollar terms, however, due mainly to repayment of the debt, the total amount of debt registered a decline of USD 207.2 m over the period from end-December 2003 to end-April 2004. In BGN terms, the amount of foreign debt increased by BGN 601.8 m. The total amount of foreign debt at end-April runs at USD 9,083.4 m or BGN 14 870.4 m recalculated at the BNB rate of BGN against the US dollar as of 30 April 2004.

There are slight changes in the debt structure as compared to the final quarter of last year. The Euro-denominated debt accounts for 36.4 per cent (against 36.9 per cent at end-December), and the debt in US dollars and other foreign currencies accounts for 47.5 per cent (47.2 per cent as of 31 December 2003) and 16.1 per cent (16 per cent at end-December), respectively. The interest structure is also subject to very slight change. The ratio between floating interest rate debt and fixed interest rate debt is 62.4 per cent to 37.6 per cent. The weighted average residual term of the debt has been lowered to 9 years and 8 months, while a certain reduction has been registered in the share of debt of 5-to-10 year maturity and an increase in the share of debt with a maturity of 10 years and more. The largest share is that of debt in other bonds - global and Eurobonds (28.3 per cent) and Brady bonds (amounting to 25.7 per cent). The share of debt to the IMF increases slightly, reaching 13.2 per cent. Loans to the World Bank amount to 11.8 per cent, government-guaranteed borrowings – to 5.9 per cent, payables to the EU- to 4.6 per cent, and to the Paris Club- to 2.6 per cent.

At the end of June **the Bulgarian government announced that on 28 July 2004 it would exercise its right of repayment before maturity of discount Brady bonds (DISCs) with par value of USD 679.3 m**, issued in compliance with the Agreement with the London Club private creditors of 1994. The Bulgarian government's decision follows the general guidelines of the Strategy for Government Debt Management adopted last year. The Ministry of Finance justified its decision by explaining that the early repayment would result in a decrease in the amount of foreign government debt and lower expenditures for government debt servicing over the next 20 years; furthermore, the foreign currency and interest structure of the debt will be balanced and the interest and principal collateral will be freed. The resources needed to carry out the operation in net terms amount to about USD 400 m from the fiscal reserve; this is so because after buying bonds back the amounts maintained as collateral for interest and principal will be freed. Projected proceeds from the freed collateral (at market value as of 24 June 2004) are in the amount of about USD 283 m.

This buy-back using funds from the fiscal reserve is a reasonable move inasmuch as interest costs on servicing the Brady bonds exceed the interest proceeds on funds in the fiscal reserve. The decision for early repayment of this particular type of debt is justified from the point of view of the provision in the Agreement with creditors stipulating that the interest on discount bonds would be increased upon reaching 25 per cent GDP growth as compared to 1993 levels. Even under the scenario that is most favourable to the country (GDP calculated at constant prices in BGN), this clause is expected to become effective in 2005, which calls for urgent measures to be undertaken. In broader terms, however, there remains the issue of the most advantageous use of the considerable fiscal reserve surplus above the required minimum needed to guarantee foreign debt payments. The early repayment of government debt is just one of a number of possible solutions which are expected to have positive effect on the country's economic development. The issue of utilizing a portion of the surplus to finance active policies aimed to boost economic growth and attract investment remains open to discussion.

Domestic debt

As of 30 April 2004, according to data from the Ministry of Finance, the domestic debt amounts to BGN 2 462.3 m. Compared to end-2003, it marked an increase in the total amount of domestic debt by BGN 221.2 m.

Within the structure of domestic debt at end-April 2004 the share of government securities issued for financing the budget deficit accounts for 79.2 per cent (against 76 per cent at the end of December 2003) of the total amount of the domestic debt. At the end of April the share of debt on government securities issued for financing structural reform amounted to 20.8 per cent (against 24 per cent at the end of last year) of the total amount of the domestic debt. Table 8 illustrates the dynamics of the total domestic debt structure.

Table 8. Total domestic debt structure (%)

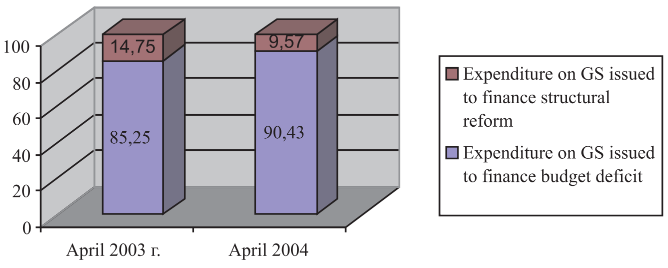
Debt structure	As of 30 April 2003	As of 31 December 2003	As of 30 April 2004
Debt on government securities issued to finance the deficit	73.9	76.0	79.2
Debt on government securities issued for the structural reform	26.1	24.0	20.8
Domestic government guarantees	0.04	0.0	0.00

Source: According to MoF data, Government Debt monthly bulletins

Total expenditures on the domestic debt (interest and discounts) as of the end of April 2004 amount to BGN 51.9 m. (against BGN 58.8 m for the first four months of the preceding year).

Against the background of these expenditures the share of expenditures on government securities for financing the budget deficit is 90.4 per cent (against 85.25 per cent at the end of April 2003). Highest is the relative share of expenditures on 5-year bonds (41.4 per cent) followed by 7-year bonds - 20.5 per cent and 3-year bonds - 14.7 per cent. The share of expenditures on government securities issued to finance structural reform is 9.6 per cent (against 14.75 per cent for the same period of 2003). Figure 6 illustrates the dynamics of the domestic debt expenditures structure during the first four months of 2003 and 2004.

Figure 6. Expenditure structure of domestic debt (%)



Source: According to MoF data, Government Debt monthly bulletins

According to BNB and MoF data ("Government Securities Market" published by Fiscal Services Department and "Government Debt" bulletin) during the first four months of 2004 the average yield attained in the primary market on newly issued government securities for financing of the budget deficit is 2.52 per cent an annual basis for three-month treasury bills (four auctions during the period), 3.55 per cent for twelve-month treasury bills (one auction during the period), 3.27 per cent for three-year bonds (one auction during the period), 4.65 per cent for five-year bonds (two auctions during the period), 5.02 per cent for seven-year bonds (one auction during the period) and 5.39 per cent for ten-year bonds (two auctions during the period).

Thus, with regard to the domestic debt market, the end of April 2004 marks a decline in the yield of all newly issued government securities compared to the end of 2003. In comparison to the end of the third quarter the share of securities issued for financing the structural reform has slightly decreased at the expense of the share of securities issued to finance the budget deficit. In comparison to the first four months of last year, the share of expenditures on government securities issued for financing of the deficit increased, while the share of expenditures on securities related to the structural reform dropped down as a consequence of the changed structure of domestic debt.

In early February the Ministry of Finance placed on the market government securities denominated in Euro and intended for direct sale to natural persons. They yield fixed income in the form of interest payable every six months as of the date of issuance; the final interest payment is made at maturity along with the par value of government securities. In order to promote savings, the interest rate increases from 4 per cent at the first interest payment to 6 per cent at the final interest payment. The issue has a five-year maturity. All payments on the issue are made in Euro, with the minimum quantity for each purchase being EUR 10. Citizens may sell back to the MoF government securities in their possession on the dates of interest payments, at a price equal to their par value. By the end of 2004 year the Ministry of Finance will place on the market five more similar issues of securities.

Floating interest rate government securities were placed on the market in February through a BNB organised auction-type sale. This was the first floating coupon issue of government securities for 7 years in view of the need to develop a secondary market for government securities, to enhance the inter-banking market and also in response to primary dealers' demand for this type of instruments. The issue was made within the limits specified in the 2004 State Budget Act and in compliance with the target stipulated in the Strategy for Government Debt Management to develop the domestic government securities market. Securities have a 3-year maturity and amount to a total of BGN 100 m; securities worth BGN 20 m were offered at the first auction. Interest is paid every three months (as of the date of issue) in the amount of the average 3-month SOFIBOR for a duration of 20 working days prior to the start of the interest period. Respectively, the amount of the interest coupon is announced by MoF no less than 3 working days after the interest period has commenced. SOFIBOR was chosen as the base of the floating interest rate in order to boost the liquidity of the monetary market and, respectively, confidence in this fixing to promote its wider use as an interest rate indicator in the financial market.

New financing

During the first four months of the year new loans totalling BGN 293.4 m were received, against total foreign debt payments of BGN 595.3 m. The payments include repayment of principals in the amount of BGN 267.5 m and interest payments of BGN 327.8 m.

On 4 February 2004 the IMF Board of Executive Directors formally finalised the fourth, last review on implementation of the Bulgarian government's economic program within the two-year stand-by agreement. The Board's decision allowed for the next disbursement in the amount of 26 m Special Drawing Rights (SDR) (about USD 38.7 m) The positive decision was justified with the stable macroeconomic indicators achieved, the introduction of a prudent and flexible fiscal policy and the establishment of the necessary preconditions for higher economic growth. The IMF stated that regardless of the increased external challenges and risks the country has achieved further progress in strengthening the principles of market-oriented economy and has undertaken substantial financial and economic reforms clearly targeted to facilitate the process of European integration. In the second half of the year a new precautionary agreement between Bulgaria and the IMF is expected to be signed.

An agreement with the World Bank was signed in April providing for the disbursement of a grant to Bulgaria in the amount of USD 495 000 which will assist the country in the preparation of the Third Program Adjustment Loan (PAL 3). The funds were secured with the financial support of the Japanese government. PAL 3 is the third from a series of program adjustment loans with which the World Bank assists Bulgaria in carrying out the planned reforms in various areas of economic and social development. The funds granted will contribute to:

- launching reforms in institutions of key importance to the labour market development which will provide flexible employment and set the necessary conditions for job creation;
- improving the social security system;
- further modernisation of the education system and health services aiming to improve quality, access and efficiency;
- promoting the central and local authorities' efforts for improvement of the social assistance system so that it can reach the most disadvantaged groups, provide social services to marginalized groups and develop alternative services to guarantee children welfare.

An Agreement for the disbursement of the Second Program Adjustment Loan PAL 2 was signed with the World Bank on 17 June 2004. It aims to support the balance of payments, economic growth and job creation in the country. The loan is worth USD 150 m or EUR 123.7 m. The amount will be paid in two disbursements. The first one amounts to EUR 103.7 m and the second amounts to EUR 20 m. PAL2 is a 17-year loan with a 5-year grace period. It aims to support the efforts, undertaken under PAL1 and to assist in the implementation of key reforms to improve the management of the country's public sector. The PAL Program's key objectives are to achieve an average annual economic growth of 4.5–5 per cent during the 2002–2005period, reduce unemployment to 18.1 per cent in 2001 and to 12–14 per cent in 2005 and substantial progress in the EU accession process. Most requirements have already been met. Key obstacles are related to the delayed finalisation of the privatisation process in Bulgaria.

Regulatory framework development

In early June the National Assembly approved on second reading **amendments to the Corporate Income Tax Act** (CITA) proposed by the Council of Ministers in connection with the European Union membership negotiations and the closing of Chapter 4, Competition Policy. Technical consultations had established that part of the fiscal measures of state aid (including tax relief), which were defined as incompatible, will have to be abolished while the remaining part should be brought in line with the *Aqcuis communautaire* in the area of state aid.

According to the amendments, the corporate tax reduction as per Art. 60, Para. 1 and the ceding of corporate tax as per Art. 61d. and 61e. will be valid when the conditions are in place for regional development state aid under the State Aid Act (SAA) and its Regulations, provided that:

- the reduction/ceding is invested for the acquisition of fixed assets, know-how, licenses and patents;
- the value of non-tangible assets does not exceed 25 per cent of the value of fixed tangible assets;
- at least 25 per cent of the value of acquired assets is financed from own funds;
- assets are to be acquired at regular market conditions compliant with the provisions for non-related parties;
- assets remain in the person's ownership for a duration of no less than 5 years as of the date of acquisition.

Another provision is introduced according to which if during the implementation of an investment project the total amount of each tax reduction and/or ceding exceeds BGN 75 m this will necessitate the issuance of a permit by the Commission for the Protection of Competition (CPC) for the admissibility of state aid. The total amount of relief and/or ceding which must be invested as an initial investment has been limited, thus guaranteeing compliance with the maximum compatible amount of aid according to the individual characteristics of the project.

An amendment **to § 60 of the Transitional and Final Provisions of the Act on Amendments to the Corporate Income Tax Act** and respectively its Regulations were also adopted[28] for the period until 31 December 2006, because this measure represents incompatible state aid. Persons (foreign investors) who were entitled to corporate tax relief also for 2007 pursuant to the revoked Art. 20 of the Foreign Investments Act were not recompensated by allowing them to cede a higher portion of corporate tax due for 2006.

Fiscal measures related to deferral and extension of tax and other public liabilities as defined in the Tax Procedure Code are now stipulated as a general measure applicable to all economic agents on the territory of the whole country. The precise conditions, criteria and indicators which provide for allowing the deferral/extension have been defined, thus abolishing the discretionary power of the competent body. Thus the competent body may issue a refusal only in the event of non-observance of the conditions and criteria or in case of non-compliance of indicators with actual market conditions.

28 Promulgated Official Gazette, issue 119 of 2002; am. iss. 109 of 2003.

The first months of 2004 are a period of dynamic and generally positive changes in Bulgaria's social sphere. Unemployment is decreasing, but this is not accompanied by parallel increase of incomes and improved standard of living. The Ministry of Labor and Social Policy demonstrates management and administrative capacity to develop and efficiently implement modern policies pursuing long-term goals. Important legislative amendments to the labor and social security legislation are in place as well. At the same time, health policy results and changes are utterly unsatisfactory; the perspectives of continuing the healthcare reform remain unclear.

Employment and Unemployment. Labor Market Policy

The first months of 2004 are characterized by continuing decrease in the number of registered unemployed. In May 2004 the relative share of unemployed in the economically active population stood at 12.6 per cent. In this aspect the objectives set in the Strategy for Employment in Bulgaria, 2004 – 2010 do not seem unrealistic. **Prevention** will be very important for attaining these goals **– this means implementing a labor market policy preventing the increase in the number of long-term unemployed and the need of social assistance.** The successful implementation of such tasks in the next years will be an indicator of the orientation of Bulgaria's social policy towards implementation of modern approaches and European policies.

For 2004 the Ministry of Labor and Social Policy plans to include not less than 18 per cent of the long-term unemployed in literacy courses, vocational training courses, as well as to provide sustainable employment for these people. A special focal point in government's employment policy will be the efforts to ensure employment for the people with disabilities by providing incentives to employers and for the unemployed young people up to 29 having no experience, education or profession. **Overall, the 2004 National Action Plan for Employment envisages provision of jobs for over 112 000 people, as well as learning and vocational training for over 47 000 people.** In addition to existing programs, other special employment programs are developed; they may provide employment to a limited number of unemployed, but help them to preserve their professional skills and experience and later to get back on the labor market.

The special programs and projects developed to promote the entrepreneurship in minority groups should be given a very positive assessment. Finance from donors and from the Bulgarian government is secured for their implementation and funds will be spent along three lines:

- Construction, urbanization and creating temporary employment;
- Vocational training of unemployed from the ethnic minorities;
- Creating permanent employment by providing incentives and support to the business under the JOBS project.

A new point in government's employment policy is the attempt to achieve an even higher degree of alignment with the European best practices in the field and **higher goals and quality results, which means decreasing the wide regional variations in employment, encouraging the labor activity at higher age, improved labor market adaptability and mobility, etc.**

To attain these goals, it will be very important to get the business involved in MLSP's programs and projects in partnership with local authorities and non-government organizations.

Incomes and Living Standards

Despite the improvement registered in employment, the incomes and living standards of Bulgarians remain low with no signs of noticeable improvement in a close perspective. The official statistics for the first months of 2004 shows a negative growth in the real monthly wage of the employed and continuing downward growth rates in the income per household member against the same period of 2003. This trend is a result of the noticeably higher inflation rates, yet obviously the increase in nominal income is not sufficient to maintain high growth rates of real income.

On the other hand, the results of other surveys and sources, which are rather based on subjective information and sociological survey assessments, do not support the above findings. For example, the "consumer confidence" indicator registers increase of 3.8 percentage points from January to April 2004. According to NSI's regular survey again, consumers' opinions of the changes in the financial situation of households in the last 12 months, as well as their expectations about the next 12 months are more favorable. Change for the worse in the balance of family finance against the previous three months by groups of persons is registered for: in terms of the employment status – the unemployed; in terms of the age group – people between 16 and 29 and 50 to 64; in terms of education – people with elementary and primary education.

Stabilization and slow growth in the consumption of households continued in the first quarter of 2004. According to the panel sociological surveys, consumption registers increase of about 7 per cent in terms of quantity against the same period of 2003. Growth in value terms is about 3–4 per cent. **The asymmetric trends in incomes indicated by different sources are explainable by the continuing high share of the informal economy and the income it generates.**

Social Assistance and Curbing Poverty

Despite the stable macroeconomic environment and GDP growth observed in recent years, far from all Bulgarians feel improvement in their living standards. **Many surveys reveal sizeable poverty niches concentrated in ethnic groups, rural regions and the unemployed.** Per capita income of Bulgarians is low at 28 per cent of the EU average. Hence it is very important to successfully implement the **National Plan for Curbing Poverty and Social Exclusion** adopted by the Government in January. It implies adequate division of responsibilities between the state, the social partners, and the citizens and the objective is to implement an integrated economic and social approach to social protection. The objectives and measures laid down in the plan are financially secured and provide for a selective approach with special focus on risk groups and priority of employment programs.

Defining officially the "poverty threshold" for Bulgaria will be important for the success of such program documents and the Ministry of Labor and Social Policy has set this as a priority in its 2004 program. It will allow measuring at higher accuracy the parameters of poverty in Bulgaria; a wide public debate will be necessarily generated and public consensus will be needed, which will finally contribute for more purposeful and efficient spending of the funds for poverty curbing measures.

The successful implementation of the Social Services in Return for New Jobs Project is an example of a modern approach towards social problems. The project offers alternative social services and provides employment to one of the most vulnerable groups on the labor market – the people of pre-retirement age. In 2004 social services will be provided to 1400 underprivileged people with the aid of almost 500 social assistants. A positive development in this case is the involvement of local non-government organizations in project implementation which will allow them to accumulate experience and skills in social services and take up this activity in the future.

Social Partnership and Industrial Relations

In the first months of 2004 the privatization and restructuring of enterprises and productions of national importance brought in higher dynamics and changes in the government-syndicates-employers relationship. In addition to the pending problems with the payment of agreed wages and the demands for higher pay (Terem, Bulgaria Air) social tension is also generated by the future changes in employment as a result of expected privatization (electricity distribution companies, Bulgartabac Holding, BTC). It is natural for the syndicates as representatives of the workers and employees to manifest high interest and defend their positions of being involved in solving these problems. Previous results indicate a reasonable and productive approach by all process actors, cooperative behavior of the syndicates, which results in the long run in mutually acceptable solutions achieved through the social dialogue mechanisms. The question is about developing and implementing in each specific case an adequate compensatory mechanism providing opportunities to alleviate social after-effects (for example, a single payment allowance for laid off workers, conditions for alternative employment, re-qualification, training, etc.).

Following lengthy discussions and procedures for verification of the national level strength and representation of social dialogue actors, in March – April 2004 the Government adopted an official decision on the strength of which five employer's and two worker's organizations are representative on national level. These include: Bulgarian Chamber of Commerce and Industry, Union of Private Entrepreneurs "Vazrazhdane" Union of Private Economic Enterprise, Bulgarian Industrial Association and Union of Employers on one part, as well as LC Podkrepa and CITUB on the other part.

A new point in the social policy is MLSP's intention to develop a **National Strategy for the Equal Opportunities for Men and Women.** While the Act on Protection against Discrimination is already a fact, an operating system for guaranteeing the equal opportunities and a structure to monitor and direct this process still need to be set up. It is a commitment of the Government to build in cooperation with non-government organizations a new type of gender partnership based on the equal involvement of women in the decision-making process and in the labor market (equal pay for equal work, improved working conditions)

An important focal point of industrial relations in 2004 is the **need to establish special industrial tribunals in Bulgaria.** While Bulgarian legislation has been modernized and aligned with European requirements, there is still a need to create a mechanism to settle labor disputes between workers and employers in an efficient and lawful manner. Labor disputes register increase in recent years, yet their consideration and settlement takes one to three years. As a way out of this situation, intensive work on studying the opportunities for the set up of special industrial tribunals and the necessary statutory and institutional changes is going on. The Ministry of Justice is expected to prepare a final report by year end and to nominate magisterial precincts for pilot projects.

In the first half of 2004 major legislative changes in the social sphere included **passing of Act on Guaranteeing the Claims of Workers and Employees in the Event of Insolvency of Their Employer; amendments to the Act on the 2004 Budget of State Social Security and two new ordinances of the Financial Supervision Commission – Ordinance on the Terms and Procedure of Licensing Actuaries of Pension Insurance Companies and of PIC-Managed Supplementary Pension Insurance Funds, and Ordinance on the Custodian Banks under the Social Security Code. The amendments to the Labor Code** passed by the Parliament on 3 June 2004 in relation to Bulgaria's commitment to fully align Bulgarian labor legislation with the *acquis* and the Europe Association Agreement were undoubtedly the most widely discussed topic in the public space.

The Act on Guaranteeing the Claims of Workers and Employees in the Event of Insolvency of Their Employer, passed by the Parliament on 21 April 2004, ensures **minimum level of protection of workers and employees in the event of insolvency of their employer. An important aspect of this act is the fact that it does not increase the social security burden for employers,** which would have increased their labor costs and would have generated possible negative social after-effects for the employees and for the labor market in general. A guarantee for the purposeful spending of the assets in the **new NSSI's Fund for Guaranteeing the Claims of Workers and Employees** is the provision that the fund's assets and liabilities cannot be consolidated with the assets and liabilities of other NSSI funds.

The act provides for a **highly restrictive investment activity of the Fund in the event of available temporary idle assets,** which guarantees the necessary protection of the insured workers and employees and constitutes a positive element in the initial period of operation of the fund. Within the meaning of the law, temporary idle assets can only be invested in government-issued or government-guaranteed securities (not less than 65 per cent of temporary idle assets), in municipal bonds (not more than 10 per cent of temporary idle assets) and in bank deposits (not more than 25 per cent of temporary idle assets). With a view to provide workers with a higher level of social protection in the event of insolvency of their employer, a gradual liberalization of the fund's investment activity could be speculated.

The Act on Guaranteeing the Claims of Workers and Employees in the Event of Insolvency of their Employer evoked different responses from employer's organizations. Some of them believe that instead of creating a fund for guaranteeing the claims of workers and employees it would be better to find a way to have wages paid on a regular basis. The main reason for the negative responses lies in the fears of diluting the responsibility. Other employer's organizations are happy that the new fund will not be within the Unemployment Fund and the insurance will cover only the enterprises that could be declared bankrupt.

The compulsory registration of labor contracts at NSSI and the minimum social security thresholds by economic activities and occupational categories introduced since the beginning of 2003 are another important form of social protection of workers and employees. **According to NSSI's data, 1 506 977 new labor contracts were registered from the beginning of 2003 till 10 February 2004**. The number of **labor contracts terminated** in the period under review is also significant **– 1 152 853**, which means that **in this period labor contracts registered at NSSI have increased by 354 124** (1 506 977 - 1 152 853). The higher number of insured persons is a necessary precondition for higher State Social Security proceeds, hence for solving the problem with the Pension Fund deficit. **The average monthly income for social security purposes registers increase of over 9.7 per cent**[29] for the period January 2003 – April 2004, which generates optimistic expectations about eliminating the Pension Fund deficit and possible lower social security burden for employers and employees in the future.

The idea of the ex-minister of labor and social policy Lydia Shuleva to make the compulsory minimum social security thresholds minimum wages for the corresponding economic activities and occupational categories became a fact for the workers and employees in the construction sector. **In April 2004 the representatives of the employers and the syndicates in the construction sector were the first to negotiate minimum wages equal to the minimum social security thresholds.** The new collective agreement signed by the Bulgarian Building and Construction Chamber and the Bulgarian Industrial Association on the part of employers and the Construction, Industry and Water Supply Federation at Podkrepa and the Federation of Independent Trade Inions in the Construction Sector at CITUB on the part of workers and employees covers 1400 construction, production, design, public utility, and investment companies. The idea of the employer's and trade union organizations in the sector is to keep the highly qualified master-builders some of whom are looking for jobs abroad, with a view to avoid future import of labor.

The intensified signing of collective labor agreements by enterprises and sectors observed in the last two years is a proof of the improved industrial relationship of Bulgarian employers and syndicates. **Data by the General Labor Inspectorate (GLI) show that over 1 700 collective labor agreements were signed in the first five months of 2004 – nearly as many as for the whole 2003.** The increasingly higher number of signed collective labor agreements, which is in the interest of both employers and employees, indicates that the Bulgarian business and labor now cooperate for the purpose of building a more efficient labor market, hence a more efficient market economy.

On one part collective labor agreements provide higher social security and stability for workers and employees, and on the other part they are an efficient tool for employers to combat the grey economy; provide uniform standards for workers and employees; make syndicates committed to complying with the labor legislation; keep the qualified personnel and guarantee the social peace. It can be assumed that the interest of employers in signing collective labor agreements will increase in the future, having in mind the Parliament-approved amendments to the Labor Code related to the requirement for employers to consult the representatives of workers and employees in the event of planned lay-offs and to make efforts to come to an agreement

29 Source: NSSI.
Note: The average monthly income for social security purposes announced by NSSI is BGN 276.08 for January 2003 and BGN 302.89 for April 2004.

with them with a view to avoid or limit planned lay-offs and to alleviate their after-effects.

The passed Act on the 2004 State Social Security Budget introduces since the beginning of 2004 stricter requirements for acquiring the right to pregnancy and childbirth benefits and to benefits for raising small children - 6 months length of service for social security purposes, of which 3 months within a year before the month of the pregnancy and childbirth leave. The different legal requirements for the minimum length of service for social security purposes which gives the right to benefits for temporary disability as a result of general illness and to benefits for pregnancy, childbirth and raising small children, as well as the adverse after-effects the amendments might have in some cases for pregnant women and for mothers raising small children were the major reasons for the Parliament to pass **Addendum to the Act on the 2004 Budget of State Social Security. The deputies delayed by six months the enforcement of the above stricter requirements with a view to find within this period a comprehensive solution for the issues related to the rights of pregnant women and mothers.**

The Amendments to the Labor Code passed by the parliament in early June evoked serious concern in the business. These amendments are generally focused on introducing new legal provisions or supplementing existing provisions, related to:

- prohibition of discrimination (direct and indirect) and establishing equality of men and women in the performance of their rights and obligations arising from labor relations;
- ensuring stability of labor relations in the event of change of ownership of enterprises;
- comprehensive regulation of the labor contract elements;
- guaranteeing equal rights and obligations for part-time employees and employees with fixed-term labor contracts with those for full-time employees and employees with permanent labor contracts;
- regulating an inter-day rest within the duration of the weekly rest;
- regulating the right of parental leave for each one of the parents taking care for children up to 8 years and the leave for pregnant workers and employees for medical examination during pregnancy;
- similar regulation of the requirements related to the special protection of pregnant workers and employees and the special protection of suckling mothers.

The questions raised by the business following the amendments to the Labor Code reveal that **some of the voted new texts in the act need to be specified and/or supplemented with a view to improve the legal regulation in this field.** One of the most widely discussed new texts in the act concerns the obligation for employers “to make efforts” to come to an agreement with the representatives of the workers and employees with a view to avoid or limit planned lay-offs and to alleviate their after-effects. The act does not specify the methods of complying with this requirement.

Labor Code amendments prevent employers from appointing new workers and employees in an enterprise with night shifts before they have arranged for a medical examination for them. The business wants to know what this examination should include and whether its result could influence the appointment of the new worker or employee. Since 1 August 2004 employers will be obliged to release from work for their account pregnant workers or employees for medical examinations when the examination needs to be made within office hours, but the law does not specify who shall determine the need of such examinations, its frequency and duration. The business expects for the so-called “parental leave” to generate serious technical problems in the human resource departments of companies, because the Labor Code does not regulate the method of calculating the leave of each parent if the two of them work in different companies, change their job, the company goes bankrupt, etc. Some business representatives believe that the voted amendments to the Labor Code limit their opportunity to extend working hours or days for production purposes.

The questions raised by the business on the newest texts in the Labor Code reveal that the representatives of the Executive, the employer’s organizations and the syndicates need to continue discussions on labor legislation problems. Besides, **further amendments to this act are expected by the end of 2004.** The Government has undertaken commitment before the EU to eliminate since the beginning of 2005 the additional payment for length of service (the so-called seniority pay), to facilitate appointment and dismissal from work, to eliminate the benefits for harmful working conditions, with employers investing instead in improved working conditions.

At the end of April 2004 CITUB sent an open letter to the National Council of NMSS where the syndicate **puts forward 23 demands** for changes in the social and economic policy of the ruling majority. Major proposals for changes in the social security domain include:

- increasing the minimum guaranteed income to not less than 50 per cent of the determined poverty threshold since 1 October 2004;
- fixing the social pension at 1.1 percent of the minimum guaranteed income since 1 January 2005;
- increasing the minimum pension for social security and old age purposes to not less than BGN 75 since 1 January 2005 and increasing the weight of the length of service for social security purposes by changing the coefficient in the pension calculating formula, including by allocating proceeds from privatization for higher pensions;
- updating pensions on an annual basis till 2006, taking into account 50 per cent the inflation and 50 per cent of the

growth in the average income for social security purposes for the previous year;

- preventing a higher total social security burden and preserving its distribution between employers and employees at a ratio of 75:25 for 2005 and 2006;
- introducing per hour calculation of the length of service for social security purposes for workers and employees on labor contracts throughout the whole life of work with a view to better guarantee the social security of flexible employment;
- expanding sector and industry labor contracts to cover all economic subjects in the sector (industry) and making the minimum social security thresholds minimum wages by corresponding economic activities and occupational categories;
- criminalizing labor and social security legislation violations by way of amendments to the Criminal Code and the Criminal Procedure Code.

A large portion of syndicates' proposals are reasonable. The question is about the proposals for increasing the weight of the length of service for social security purposes in calculating pensions, allocating proceeds from privatization for higher pensions, updating pensions on an annual basis with an appropriate coefficient, introducing per hour calculation of the length of service, and wider coverage of sector and industry collective agreements. **Yet to make these social changes a reality, there is a need of wide public debate and consensus involving employer's organizations and representatives of the Executive, of non-government organizations and of the academic society,** because the problems and possible changes in the pension system concern all Bulgarians.

On the other hand, there are proposals that contravene the Social Security Code and generally the idea of the Bulgarian pension model, which is very well designed but difficult to realize in time. The question is about keeping the division of the social security burden between employers and employees (75:25) in the next two years – 2005 and 2006.

The high amount of the total social security burden is a major reason for the sizable deficit registered every year in the Pension Fund. While social security proceeds to NSSI have registered increase as a result of the minimum social security thresholds by economic activities and occupational categories and the compulsory registration of labor contracts at NSSI introduced since the beginning of 2003, the public space has not witnessed yet any serious debate on decreasing the total social security burden for employers and employees. Allocating a portion of the proceeds from privatization to finance current pensions may be a solution towards decreasing the total social security burden, yet there is a need to seriously analyze the benefits and losses of one or another investment decision.

Supplementary Pension Insurance

Data about the insured persons and the available net assets of pension funds as of 31 March 2004 reveal **that in the first quarter of 2004 as well the number of insured persons and the amount of the available net assets in UPFs register the highest growth (+2.00 per cent and +22.47 per cent accordingly). Total insured persons in pension funds have increased by 29.03 per cent** against 31 December 2002 (i.e. **within 15 months),** with UPFs registering again the highest growth (+41.37 per cent). **For the same period the net assets of pension funds register increase of 70.59 per cent and stand at BGN 567 162 thousand at the end of March 2004**, with UPFs registering the highest growth in their assets (+234.95 per cent). Assets of privately managed UPFs, OPFs and VPFs are a huge financial resource that needs to be attracted to the real sector with a view to improve the competitiveness of Bulgaria's economy.

The upward trend of the relative share of assets in UPFs in aggregate pension assets at the expense of the relative share of assets in VPFs, established in 2003, continues, which is a result of the increasingly higher number of insured persons in UPFs and the increase of the social security contribution to UPF from 2 to 3 per cent since the beginning of 2004. The relative share of assets in UPFs register increase from 12.54 per cent at the end of 2002 to 22.34 per cent at the end of 2003 and 24.63 per cent at the end of March 2004. Against this increase, the share of the assets of VPFs in the aggregate pension assets registers continuing decrease from 58.81 per cent at the end of 2002 to 49.49 per cent at the end of 2003 and 47.61 per cent at the end of March 2004. The share of the assets of OPFs in the aggregate pension assets registers decrease as well, however at lower rates (from 28.65 per cent at the end of 2002 to 28.17 per cent at the end of 2003 and 27.76 per cent at the end of March 2004).

As at end of March 2004 PIC Doverie AD has managed to attract the highest number of insured persons (42.24 per cent). This pension company accounts for the highest share of insured persons in UPFs and OPFs - 46.96 per cent and 42.36 per cent accordingly. In terms of the share of insured persons in VPFs, only PIC Allianz Bulgaria AD (49.01 per cent) registers improved market positions against PIC Doverie AD (27.14 per cent). **In terms of the market share in pension assets PIC Doverie AD (31.87 per cent) gives in to no one but PIC Allianz Bulgaria AD (38.24 per cent)**. It should be noted that three of the eight pension insurance companies **(PIC Doverie AD, PIC Allianz – Bulgaria AD and PIC Saglasie AD) hold over 80 per cent of total insured persons in UPFs, OPFs and VPFs and over 80 per cent of total pension assets,** which indicates significant concentration of the pension services market.

The campaign for transfer of insured persons from one supplementary pension insurance fund to another, which started in early 2004, is a chance for smaller pension insurance companies to increase their market share. Experts expected that not more than 5-10 per cent of the insured persons would change their pension fund. FSC's data about the number of insured persons who changed their pension fund in the first quarter of 2004 reveal that at this stage **insured persons are not highly interested in changing their pension fund.** Insured persons in OPFs who have changed their pension fund account for the highest share (3.44 per cent). The share of insured persons who have changed their UPF or VPF stands below 0.1 per cent (0.83 per cent of the insured persons in UPFs and 0.51 of the insured persons in VPFs). It can be assumed that the so-called accounting shares to be introduced by pension insurance companies since 1 July 2004 will increase the interest of insured persons in changing their pension fund because they will have day-to-day information about the yield on the invested social security assets of the pension fund they have chosen and they will be able to compare it to the yield achieved by other funds.

FSC's data about pension funds' investments as at the end of March 2004 reveal that **government-issued and government guaranteed securities as well as national bank deposits and mortgage bonds remain the basic financial instruments in which pension assets are invested**. Despite that, notable is the higher diversification of the assets in the investment portfolios of pension funds. Pension funds invest increasingly higher amount of assets in shares and corporate bonds, which is a sign that the potential of pension assets to improve the competitiveness of Bulgarian enterprises is being used. Pension companies insist on having the threshold on universal and occupational pension funds' investments in government securities lowered from 50 per cent to 30 per cent and on being allowed to form portfolios with diversified investment risk which insured persons should choose depending on whether they are close to retirement age or not.

Neither UPFs, nor OPFs or VPFs invested abroad in the first quarter of 2004. A possible explanation of this fact is the good yield pension funds have achieved on investments in Bulgaria. As at the end of March 2004 UPFs and OPFs register average annual yield of 12.44 per cent and 11.47 per cent accordingly. As at the end of March 2004 the net annual yield of VPFs for the previous 12 months varies by funds between 7.62 per cent and 11.27 per cent. Insurance in private pension funds remains a good investment given the 2003 inflation rate (5.6 per cent) and the 2003 average annual interest rate on deposits in BGN (5.38 per cent).

While pension funds register rather good annual yield as of end of March 2004, 12 pension funds report negative yield for May. According to FSC's data, the negative result of pension funds' investments for May 2004 totals BGN 836 thousand. Voluntary funds register the highest negative yield (BGN -518 thousand), followed by occupational funds (BGN -179 thousand) and universal funds (BGN -139 thousand). According to experts in the field the negative yield achieved in May is basically attributable to the lower debt securities quotations and to the market price based assessment of the corresponding issues in pension funds' portfolios. In their opinion the current situation on this market does not give any idea of pension funds' investment strategy, which should be assessed employing wider investment horizons of two – three years.

At this stage pension funds generally invest in fixed yield securities and in bank deposits, which while bearing low risk, are influenced by global debt markets. The negative yield achieved by the 12 pension funds in May brings forward again the question of the necessary security-yield balance in investing social security assets and of higher liberalization of the investment regime on which pension companies have been insisting for more than two years. The idea of allowing pension funds to manage different investment portfolios with different risk-yield combinations depending on the individual preferences of insured persons becomes increasingly popular.

Table 9. Insured persons in pension funds

	As of 31.12. 2002	As of 31.12. 2003	As of 31.03. 2004	Variation against 31.12.2002, in %	Variation against 31.12.2003, in %	Share of insured persons by funds as of 31.03.2004
Total insured persons in supplementary pension insurance funds	1804469	2294966	2328388	+29,03	+1,46	100.00
Total insured persons in UPFs	1164482	1613875	1646205	+41,37	+2,00	70.70
Total insured persons in OPFs	155196	164943	165148	+6,41	+0,12	7.09
Total insured persons in VPFs	484791	516148	517035	+6,65	+0,17	22.21

Source: FSC, Social Security Supervision Department, as well as own estimates

Table 10. Available Net Assets of Pension Funds

	As of 31.12. 2002	As of 31.12. 2003	As of 31.03. 2004	Variation against 31.12.2002, in %	Variation against 31.12.2003, in %	Share of pension assets by funds as of 31.03.2004
Total available net assets in supplementary pension insurance funds, thousand BGN	332465	510544	567162	+70,59	+11,09	100.00
Available net assets in UPFs, thousand BGN	41705	114058	139691	+234,95	+22,47	24.63
Available net assets in OPFs, thousand BGN	95241	143817	157435	+65,30	+9,47	27.76
Available net assets in VPFs, thousand BGN	195519	252669	270035	+38,11	+6,87	47.61

Source: FSC, Social Security Supervision Department, as well as own estimates

Table 12. Pension Funds' Investments in Different Financial Instruments

Investment types	Total for UPFs		Total for OPFs		Total for VPFs	
	As of 31.12. 2003	As of 31.03. 2004	As of 31.12. 2003	As of 31.03. 2004	As of 31.12. 2003	As of 31.03. 2004
1. Government issued or government guaranteed securities	71.68	**67.97**	68.97	**70.44**	58.57	**61.35**
2. Securities accepted for trading at regulated securities markets	3.84	**7.62**	6.57	**7.43**	7.89	**7.55**
2.1. Shares	1.20	**2.60**	1.99	**2.33**	3.65	**3.78**
2.2. Corporate bonds	2.64	**5.02**	4.58	**5.10**	4.14	**3.77**
3. Municipal bonds	0.23	**0.20**	0.50	**0.42**	0.42	**0.37**
4. Bank deposits	13.15	**11.46**	16.12	**11.38**	20.51	**18.95**
5. Mortgage bonds	10.87	**12.58**	7.10	**9.69**	8.56	**8.60**
6. Investment estates	0.22	**0.17**	0.72	**0.64**	3.29	**2.96**
7. Derivatives of securities	0.00	**0.00**	0.00	**0.00**	0.00	**0.00**
8. Investments abroad	0.01	**0.00**	0.02	**0.00**	0.01	**0.00**
9. Other investments	0.00	**0.00**	0.00	**0.00**	0.75	**0.22**
Total	100.00	**100.00**	100.00	**100.00**	100.00	**100.00**

Source: FSC, Social Security Supervision Department

Table 11. Market Shares of Pension Insurance Companies as at 31.03.2004

Pension insurance company	Market share, in %									
	By number of insured persons in UPFs		By number of insured persons in OPFs		By number of insured persons in VPFs		By total number of insured persons		By net assets amount	
	As of 31.12. 2003	As of 31.03. 2004	As of 31.12. 2003	As of 31.03. 2004	As of 31.12. 2003	As of 31.03. 2004	As of 31.12. 2003	As of 31.03. 2004	As of 31.12.2003	As of 31.03.2004
PIC Doverie AD	47.07	46.96	42.37	42.36	26.98	27.14	42.21	42,24	31.74	31,87
PIC Saglasie AD	12.16	12.16	18.60	18.67	6.43	6.33	11.34	11,33	9.95	10,00
PIC DSK-Rodina AD	5.75	5.80	3.98	3.99	4.34	4.33	5.30	5.34	5.04	5.00
PIC Allianz Bulgaria AD	19.92	20.02	22.13	22.14	49.19	49.01	26.66	26,61	38.52	38,24
PIC I N G AD	8.78	8.90	3.71	3.74	3.80	3.87	7.30	7.42	6.29	6.52
PISC CKB-Sila AD	3.09	3.13	3.82	3.72	3.21	3.21	3.17	3.19	1.95	1.95
PIC LUKoil Garant – Bulgaria AD	3.24	3.03	5.39	5.38	6.03	6.09	4.02	3.87	6.51	6.42
DZI – Pension Insurance AD		0.006			0.02	0.02	0.004	0.009	0.008	0.009
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Source: FSC, Social Security Supervision Department, as well as own estimates

Table 13. Total outgoing persons from the corresponding UPF, OPF and VPF in the period 1 January 2004 - 31 March 2004

	UPF			OPF			VPF		
	Total outgoing persons	New members	Net difference	Total outgoing persons	New members	Net difference	Total outgoing persons	New members	Net difference
Doverie	8037	1565	**-6472**	1927	1695	**-232**	787	1424	**637**
Saglasie	3075	485	**-2590**	1542	657	**-885**	760	105	**-655**
DSK - Rodina	630	3045	**2415**	265	458	**193**	106	4	**-102**
Allianz - Bulgaria	989	5716	**4727**	1186	970	**-216**	928	139	**-789**
I N G	515	1378	**863**	298	976	**678**	16	708	**692**
CCB - Sila	303	747	**444**	252	121	**-131**	43	71	**28**
Lukoil Garant – Bulgaria	182	23	**-159**	203	747	**544**	5	2	**-3**
DZI	0	772	**772**	0	49	**49**	0	192	**192**
Total	13731	13731	**0**	5673	5673	**0**	2645	2645	**0**
Total insured persons as of 31.03.2004	1646205			165148			517035		
Share of transferred insured persons in total insured persons	**0,83**			**3,44**			**0,51**		

Source: FSC, Social Security Supervision Department

Mandatory Health Insurance

By June 2004 NHIF, BDU and UDB have not agreed yet on signing the 2004 National Framework Agreement. Nothing indicates that it will become a fact in the near future, which is a signal of serious opposition on the part of medical care providers to the health care reform implemented by the Executive. It is the Bulgarian patients that suffer most from the absence of NFA 2004 in the long run.

The Bulgarian Doctors Union put forward four basic issues for NHIF to solve as a condition for signing NFA 2004. These concern the new financing scheme for hospitals, the method of determining the wages of the staff in medical institutions, the requirement for electronic reporting of general practitioners and hospitals and last but not the least, the fact that 1.5 million people are not health insured. The Parliament-approved amendments to the Health Insurance Act **extend the time limit for filing applications for deferred payment of outstanding health insurance contributions till 30 September 2004.** On the other hand, NHIF representatives believe that the issues put forward by BDU are irrelevant to the subject-matter of NFA. This long-drawn-out conflict between BDU on one part and MoH and NHIF on the other part results in a lack of a new NFA for 2004, which deprives the health care system of the additional funds, budgeted for new health services in 2004.

MoH and NHIF see the development of a health insurance code as a possible mechanism of preventing such situations in the future. **The idea is to have the rights and obligations of the parties to the mandatory health insurance, the mandatory social health assistance and the supplementary health insurance regulated in the health insurance code.** The plans are to have the draft code developed by the end of 2004, passed by the present parliament, and effective since 2006. The issues to be regulated in the new health insurance code relate to defining the scope of finance of the health care system, clear division of responsibilities between the health care institutions, regulating the basic package of mandatory health care services, defining the scope of application of voluntary health insurance funds and solving the problems of the people who cannot afford to make health insurance payments.

The plan is to target the mandatory social health insurance towards people who do not have regulated income. With that end in view, a special fund with a capital of BGN 25 m will be set up at the Ministry of Labor and Social Policy to cover a specified package of health services supported from the state budget. **It is not envisaged to have the health insurance contribution increased from 6 to 9 per cent in 2005 as proposed by primary care doctors; funds for health care are expected to amount to not less than 4.3 per cent of GDP as in 2004,** despite that syndicates insist on not less than 6 per cent of GDP. Provided that the relative share of health sector funds in GDP is preserved in 2005, the amount in absolute terms is expected to register an increase of about BGN 100 m owing to GDP growth.

The MoH-conducted analysis of the condition of medical institutions and of NHIF’s expenditure for the first quarter of

2004 reveals that **Bulgarian hospitals are accumulating debts again, while at the same time NHIF registers sizable increase of the funds paid to medical institutions on clinical paths.** As at beginning of April 2004 hospitals' liabilities amount to about BGN 90 m, with supplies of medicines accounting for 70 per cent of this amount. Hospitals' overdue liabilities amount to about BGN 30 m, which means that medical institutions will have to pay penalty interest. The hospitals' debt analysis reveals that municipal hospitals are more efficient in managing the funds they receive from NHIF and MoH compared to the large medical institutions registering a higher volume of provided medical services against the budgeted volume, which is the basic reason for the accumulated higher amount of debt.

According to NHIF, the average monthly expenditure budgeted for 2004 amounts to BGN 69.073 m, while the real average monthly expenditure exceeds that amount by BGN 100 m. BGN 1.1 m above the amount budgeted for 2004 are spent for hospital care alone. **If this growth rate of NHIF's expenditure continues till year end, NHIF's 2004 over-expenditure is expected to amount to about BGN 11 m.** The two basic measures which MoH and NHIF propose with a view to regulate the expenditures of the public institution and to avoid spending funds from NHIF's reserve in BNB to cover operating payments for 2004 include introducing a precise information system and higher control on NHIF's expenditures.

During the National Conference on Emergency Aid and Hospital Finance Problems organized by MoH on 11 and 12 June 2004 it was pointed out that **emergency aid is still a buffer concealing problems in other structures within the health care system, outpatient care in the first place.** Conference participants reached a consensus on **the need to introduce economic mechanisms to differentiate better emergency outpatient care activities from primary health care activities.** Major emergency aid issues discussed at the conference included the lack of staff in the Emergency Aid Centers (EAC) and the personnel qualification, EAC – hospital relationship, the role of the emergency ward in the medical care structure and the opportunities for penetration of private investments in the system.

MoH presented a new idea at the National Conference: **Investment Program for Reform of the Hospital Care Sector through a Revolving Investment Fund**. The basic objective of the fund is to create a sustainable investment scheme for investments in the health care system based on objective analysis of needs, adequate planning and preparedness of hospitals to undertake financial commitments. The start-up capital of the fund amounts to EUR 11 m provided under the Reform of the Health Sector Project.

The National Audit Office's Audit Report on the 2003 financial management of NHIF's budget and property revealed schemes and mechanisms for draining the public institution. Getting around the Public Procurement Act in signing agreements with pharmaceutical producers and suppliers, signing agreements with out-house consultancy offices while having an in-house legal department are two mechanisms for diverting and misusing health insurance funds employed by NHIF's management. **The experts from the National Audit Office have identified six preconditions for legal deviation of assets from health insurance payments and from the funds targeted by the state towards risk social groups** – incomplete set of regulatory documents for NHIF's activity; non-transparent system of negotiating prices between NHIF and pharmaceutical producers and importers; poor control and poor contacts between the control bodies within the health care system responsible for regulating NHIF's activity; inefficient pay method for general practitioners; hospital treatment assignments creating preconditions for double payment for one and the same service by NHIF and by the patient; absence of a well-developed and established uniform accounting practice. **There is a need to take urgent legislative measures to eliminate the existing variants for draining NHIF with a view to guarantee purposeful spending of health insurance funds and to increase the confidence in the implemented health care reform.**

Voluntary Health Insurance

Two new actors appeared on the voluntary health insurance market in early 2004, which indicates higher interest in this market. Following FSC's decision to license the Health Insurance Company Bulgaria Health AD and the Voluntary Insurance Network – Health AD, licensed health insurance companies totaled 8 in number. Another 4 companies were licensed in 2003 – Bulstrad – Health Insurance AD, Health Insurance Joint-Stock Company DZI AD, Health Insurance Fund Medico – 21 AD and Bulgarian Health Insurance Fund AD. In addition, in March 2004 FSC licensed the Bulgarian Health Insurance Company Zakrila AD to provide a new health insurance package – Dental Care.

FSC's 2003 data about the voluntary health insurance market reveal that **the 2003 gross premium income from voluntary health insurance registers increase of 93.21 per cent against 2002** (BGN 6 405 thousand for 2003 against BGN 3 315 thousand for 2002). **Bulgarian Health Insurance Company Zakrila AD accounts for the highest market share (88.20 на сто) in the 2003 premium income.** It is followed by United Health Insurance Fund Doverie AD with 6.63 per cent and Health Insurance Joint-Stock Company DZI AD with 2.58 per cent. To compare, the 2002 total premium income of the two health insurance companies operational in Bulgaria in 2002 – Bulgarian Health Insurance Company Zakrila AD and United Health Insurance Fund Doverie AD amounted to BGN 3 315 thousand, with the companies holding market shares of 92.91 per cent and 7.09 per cent accordingly. **2003 honored claims**

amount to BGN 2 571 thousand against BGN 427 thousand in 2002 (registering an increase of over 502 per cent).

The 2003 results of health insurance companies reveal **a significant concentration of the voluntary health insurance market**. The two oldest companies – Bulgarian Health Insurance Company Zakrila AD and United Health Insurance Fund Doverie AD account for over 94 per cent of the 2003 premium income from voluntary health insurance, while the newly licensed companies are still in the early phase of developing their distribution network and attracting customers. The new health insurance code is expected to provide clear regulation of the scope of application of health insurance companies and to contribute to the accelerated growth of the voluntary health insurance market.

As revealed in an assessment carried out with European Union technical assistance, Bulgaria's investment and institutional costs to achieve full compliance with the environmental standards are estimated at about EUR 9 b by the year 2015; of these 30 per cent will be invested by businesses. Environment-related investments will mainly consist of funds needed for alignment with the Directives on urban waste water treatment plants, domestic waste disposal, reduction of noxious emissions into the ambient air and Water, integrated industrial pollution prevention and control.

Bulgaria will receive ISPA Program grants at the amount of BGN 100–140 m per year by 2006; after the country's EU accession this amount is expected to be increased nearly five-fold as it will include funding from the European Union's Structural Funds and the Cohesion Fund.

Compliance with the environmental *standards*

Investment needs for the private sector to achieve compliance with the environmental *standards* are projected to reach EUR 5–6 b over the 2012-2014 period. In view of the current general rate of public and private environment-related investments, the average per-annum amount will account for 2 to 5 per cent of the GDP. If Bulgaria succeeds in improving its investment climate, the country will have a great potential for attracting environmental investments by also making use of the Kyoto Protocol mechanisms. A "green investments" scheme is to be launched shortly as one of the ways to benefit from opportunities in emission trading as provided for under Art.17 of the Protocol. The Foreign Investment Agency is the government institution, which is committed to enquire into such opportunities and assist Bulgarian firms wishing to enter into public/private partnerships for the implementation of environmental projects and in particular projects employing reduced emission sales.

The second major aspect of preparing businesses for the implementation of the environmental acquis is to raise companies' awareness of the commitments made in the course of the accession negotiations. To this end, business associations, employers' organizations and the executive authorities (Ministry of Economy, Ministry of Agriculture and Forestry and Ministry of the Environment and Water) have established a Joint Advisory Council under the auspices of the Ministry of Economy. The Council will provide assistance to entrepreneurs by offering specific information on Community standards, including information related to environmental and technological requirements, which Bulgarian enterprises need to meet in pursuance of the arrangements under the Chapter "Environment".

The implementation of specific programs in support of small and medium-sized enterprises in the country is the objective of the newly launched **project** "Promotion of Energy Savings and Environment-Friendly Technologies" developed by the Ministry of Economy and the EU PHARE Program. One of the programs under the project envisages nation-wide actions aimed at drafting the legal and economic framework to provide assistance to businesses in introducing the environmental *standards***.**

Transitional periods

The transitional periods granted to Bulgaria in the course of negotiations with the European Union are among the state administration's key arguments in justifying the planned preferential treatment of national companies as they work towards full compliance with the environmental acquis. The attached information (Table 14) on transitional periods granted to the 10 new Member States as compared with those Bulgaria was granted under the Environment Chapter, reveal the declared and protected national priorities of negotiating countries.

Table 14. Transitional periods granted to the 10 new EU Member States and Bulgaria in the field of environment

Country[30]	Directives on	Year of implementation
Estonia	Urban waste water	2010
	Landfill Waste	2009
	Drinking water	2013
	VOCs from petrol storage	2006
Cyprus	Urban waste water	2012
	Packaging waste	2005
	Sulphur content in certain fuels	2005
Latvia	Drinking water	2015
	Landfill Waste	2004
	Urban waste water	2015
	Packaging waste	2007
	VOCs from petrol storage	2008
	Integrated pollution prevention and control	2010
	Asbestos Directive	2004
	Health protection against ionising radiation	2005
Lithuania	Urban waste water	2009
	VOCs from petrol storage	2007
	Packaging waste	2006
Malta	Urban waste water	2007
	VOCs from petrol storage	2004
	Air pollution from large combustion plants	2005
	Drinking water	2005
	Dumping of dangerous substances into sea	2007
	To reach overall recycling target	2005
	Recycling of Plastics	2009
	Ban of bottling of soft drinks in plastic bottles	2007

30 Information on the ten new EU Member States is from the Dutch institute EIPA, Scieberras, Anne Marie. 2002. "Challenges for the Accession Countries in the EU's Environmental Field": Eipascope 2002 (3), Maastricht.

Country	Directives on	Year of implementation
Slovakia	Hazardous waste incineration	2006
	Discharge of dangerous substances into surface water	2006
	Urban waste water	2015
	VOCs from petrol storage	2007
	Air pollution from large combustion plants	2007
	Integrated pollution prevention and control	2011
Slovenia	Urban waste water	2015
	Packaging waste	2007
	Integrated pollution prevention and control	2011
Poland	Sulphur content in certain fuels	2006
	Shipments of waste	2007
	Landfill Waste	2012
	Packaging waste	2007
	VOCs from petrol storage	2005
	Integrated pollution prevention and control /IPPC/	2010
	Discharge of dangerous substances into surface water	2007
	Health protection against ionising radiation	2006
Hungary	Urban waste water	2015
	Packaging waste	2005
	Hazardous waste incineration	2005
	Air pollution from large combustion plants	2004
Czech Republic	Urban waste water	2010
	Packaging waste	2005
Bulgaria[31]	Sulphur content in certain fuels	2009 - for gas oil 2011 - for boiler fuels
	VOCs from petrol storage	2007 - for 355 petrol stations and 50 transportation tankers 2009 - for 653 petrol stations and 466 transportation tankers
	Packaging waste	2009 - for 15% of plastics recycling 2011 - for 50% reuse and recovery of wastes
	Landfill Waste	2014 - for storage of liquid waste in 14 installations
	Control of shipments of wastes	2009
	Urban waste water	2010 - for settlements having over 10 000 residents 2014 - for settlements with less than 10 000 residents
	Integrated pollution prevention and control	2008 - for 5 installations 2009 - for 1 Installation 2011 - for 35 installations
	Air pollution from large combustion plants	2014 - for various facilities in 4 CHPPs- different transitional periods have been granted: 2008; 2010; 2014

In spite of this mechanism negotiated at government level **Bulgarian business community members have proposed additional measures** that would considerably contribute towards meeting the set targets within the arranged deadlines. Bulgarian industry representatives are generally of the opinion that the country's environmental policy should involve specific actions aiming to:

- liberalise the maximum emission levels and the negotiated air quality standards;
- review and optimise the amounts of charges, fines and sanctions - the business community's point of view being that the economic mechanisms applied in the country are stricter than the respective European requirements or the general sanction rates for EU Member States;
- alleviate or eliminate unnecessary authorisations which burden businesses with complicated and bureaucratised requirements and demotivate local and foreign investors (particularly in the sectors of chemical industry, metallurgy, and energy);
- ensure the government's assistance in developing partnerships between the public and private sector and allocating financial resources from pre-accession, structural and cohesion funds to the municipal and national budget;
- channel financial resources coming from the business sector (penal sanctions, fees) to industrial sector projects thus instead of the current practice to finance municipal projects through the "Enterprise for Management of Environment Protection Activities" (EMEPA); discard restrictions for access to information regarding the control of EMEPA funds and increase the business community's involvement in the supervision of EMEPA-financed projects (by respectively amending the Environmental Protection Act and other regulations);
- channel the financial resources allocated under Joint Implementation projects and emission trading to the pollutant enterprises which implemented the respective projects;
- ensure preferential treatment for investment in environmental technologies, programs and facilities;
- expand financial opportunities to invest in programs aiming to achieve compliance from other additional sources.

It is industrial stakeholders' belief that if government institutions fail to take efficient action to implement the proposed measures enterprises which have already begun introducing new technologies will be in potential danger of being discarded from the preferential treatment lists or forced to make incorrect investment plans.

[31] Information on Bulgaria was provided by the Ministry of the Environment and Water, available at: http:// www.moew.government.bg , last visited on 2.07.2004.

Regulatory framework

An amendment to the Environmental Protection Act contains provisions for unsettled charges and fines levied for environment and water pollution to be collected by the National Revenue Agency following the procedure as laid down in the Tax Procedure Code. The "tacit consent" concept will be abolished for cases of refusal to issue a permit related to environmental protection; furthermore, the number of enterprises which will be required to establish an accident-prevention system while operating hazardous substances will be increased. The current limit covers 70 companies processing over 5000 t of oil per year while the new amendment provides for this threshold to be lowered to 2 500 tons of oil per year.

The draft of the Act on Genetically Modified Organisms is currently in the process of second reading by the National Assembly. The draft provides for the release into the environment of genetically modified organisms and placing on the market of seeds and products containing GMO while adhering to the precautionary principle. That, in effect, means that businesses and research institutions engaged in activities involving GMO will only be granted permits following a complicated assessment-and-control procedure to ensure the prevention of adverse effects on human health and the environment. The authorisation procedure for activities involving GMO consists of several stages. Companies or research organizations planning to implement projects which involve growing or experimenting with such organisms will be obliged to notify the Ministry of the Environment and Water and submit a technical dossier and activity description. A Commission comprising of academicians, ministry officials, professional organisations and NGOs will then prepare an opinion on the application and submit it for open public discussion following its publication in the press and electronic media. Within one month of the initial publication of its opinion, the Commission will issue its final decision on the application. Based on the Commission's final decision, the Minister of Environment and Water, in coordination with the Minister of Agriculture, will issue or refuse to issue an authorisation thereby laying down the terms and conditions for the release of GMO into the environment. In its turn, upon commencement of the activity involving the release of GMO, the applicant is obligated to exercise regular control and file the information on the results and environmental risk assessment related to the project implementation. So far, activities in Bulgaria, involving genetic engineering of organisms, were governed by an Ordinance of 1996 regulating only genetically modified higher plants. Permits to companies and research units were issued under the provisions of that Ordinance. The new Act provides for existing authorisations to remain effective until the end of the current year.

With the adoption of the Genetically Modified Organisms Act this year there will finally be a legal framework in place in an area of public relations, which undoubtedly caused concerns as regards the lack of reliable and unambiguous information on existing practices. State administration however has not yet given a clear answer as to whether, by laying down the legal regulation of control over activities involving genetically modified organisms, the new Act is not, to all intents and purposes, performing another function - namely to regulate the production and trade in such organisms. Another issue of not less importance is how the adopted line of policy as regards activities involving the release of genetically modified organisms would relate to prominently declared priorities (to pursue and develop environmental tourism and organic farming and specialise in the production of organic foodstuffs) and also to the situation of current market restrictions in the European Union on products containing GMO.

A draft of the **Environmental Noise Protection Act** is already submitted for deliberation in the National Assembly. The government presented a draft law aiming to introduce an integrated approach for the avoidance, prevention and limitation of the adverse effects of noise on human health and regulate social relations as regards noise control and management. The draft law contains provisions for developing maps of noise pollution sources (including industrial ones) and drawing up action plans based on these maps. Control aimed at the prevention of the adverse effects of noise is foreseen at all levels - preventive, current and follow-up; the competent bodies to exercise such control are the Minister of Health as regards local sources penetrating into residential and public buildings, the Minister of Environment and Water and the Directors of Regional Inspectorates of Environment and Water as regards noise pollution from industrial installations, the Minister of Interior as regards the proper technical condition of vehicles, and the Minister of Regional Development and Public Works as regards noise from construction works. The Minister of Transport and Communications will be empowered to exercise control over airports, air transport and railway transport facilities. Mayors of the respective populated areas will be in charge of the organisation and control over the traffic of automobile transport through populated areas and the operation of industrial installations and facilities. The draft law provides for ensuring access to information regarding noise in the environment and the active involvement of stakeholders and the community in discussions and decision-making related to the prevention of the adverse effects of noise.

The deadline for implementation of the **product charge for manufacturers and importers of packaged goods as provided for under the Ordinance on packaging and packaging waste** became effective on 12th March 2004. The Ordinance - which should have been in force since the beginning of 2004 – caused much confusion as to its practical aspects and became the source of difficulties related to the role and official powers of customs authorities. It became the source of additional waste of time and financial resources for businesses as they attempted to fulfil their obligations laid down in the Ordinance.

In pursuance of the arrangements under the Environment Chapter, during the current year the country must reach a recycling or other treatment rate of 20 per cent of packaging waste as a step towards fulfilling its commitment which is to reach 38.9 per cent of waste recycling or other treatment by 2007. The Waste Management Act of 2003 provided for three options for companies manufacturing or importing packages. Companies can choose to conclude contracts with a recycling enterprise, form a common organisation for waste use, or else pay a product charge to the state.

Several months of implementation of the Ordinance on packaging and packaging waste demonstrated how unfit businesses were to meet the new requirements related to the implementation of European practices of waste management and use. The charge - which was only proffered as one of three forms of businesses' involvement in activities related to the use of packaging waste - was rather torpidly adopted by companies as the option requiring least efforts. On the other hand, deficiencies in the regulatory framework lead to some nerve-wracking experience with its initial implementation in early 2004. As practice has revealed, the product charge on packaging and packaging waste threatens to actually augment businesses' administrative costs. Even companies which do not manufacture packaging face difficulties as they are forced to allocate resources for intra-company control on packaging. Some very reasonable issues were raised by the business community related to VAT levying and VAT refund, the unequal treatment of small and large import companies, the practice of levying the charges using the highest tariff position for the types of materials available in shipments, the lack of clarity on the required documentation verifying the types of materials, the difficulties in processing customs and accounting documentation etc.

National business community members and business organisations' representatives voiced the well-justified warning that the current practice will contribute to creating more favourable conditions for the so-called "shadow" businesses to the detriment of legitimate ones. Another issue of interest to the business community has to do with spending the funds from the product charges already collected or now being collected. It is common knowledge that by law these are transferred to the Enterprise for Management of Environment Protection Activities and are mainly intended for financing municipal projects related to separate waste collection. Business organisations provided arguments to support an alternative position - that charges levied on packaging waste should be transferred to a separate account and should only be disbursed for projects related to waste collection and recycling; the size of charges should be reduced as currently these are on a par with the highest rates applied in EU Member States.

Following several months of experience with the implementation of the Ordinance on packaging and packaging waste, one of the most important outcomes was that within just a short time the number of businesses which chose an alternative form to achieve packaging waste recycling or other treatment grew: two waste recycling organisations were established - EcoBulPack and EcoPack - Bulgaria A third company has filed an application to set up a collective system. The experience now gained should be reviewed also in the context of European Directives 2002/96 and 2004/12 on the recycling or other treatment reuse and recovery of waste from electrical and electronic equipment which will be enforced in Bulgaria in due time. Existing good practices in this area in many European countries should be carefully analysed and introduced taking primarily into account the level of preparedness of Bulgarian manufacturers and consumers.

Bearing in mind the requirements of European Directive 2000/60/EEC regarding policies and priority actions for integrated water management, the Council of Ministers adopted **a new Strategy for the Development and Management of the Water Sector in Bulgaria by 2015.**

The Strategy foresees the adoption of a completely overhauled Water Act implementing the "pollutant pays" and "water pays for water" principles, by defining the specific conditions to preserve the Water intended to be abstracted as drinking water, major social relationships related to water services provision, the procedures for issuance of authorisation to use Water, including the facilitation of such authorisations in the interest of the general public. The introduction of public registers at the national and basin level and regular reports on the state of drinking and mineral water in the country will ensure wide public access to updated and reliable information on the sector and services available to the population.

One of the key changes reflected in the National Strategy for the Development and Management of the Water Sector is the change of ownership of water facilities and systems and the restructuring of water supply and sewerage systems and facilities. The common parts of the water supply system servicing populated areas in more than one municipality and dams regulating most of the river runoff water in Bulgaria, will continue to be public state property. The remaining parts of the system, including water conduit and sewerage networks in populated areas as well as monitoring and security facilities are envisaged to become public municipal property. The transfer of assets will be preceded by detailed research into the state of the water systems and facilities which are, or are intended to become, public municipal or public state property; an assessment of investment needs will also be conducted prior to the transfer. During that period municipalities or the state could request of the commercial companies in whose assets the water facilities and systems are included to legally transfer these assets making them public municipal or public property; for these, too, assessment will be carried out to establish their current state and investment needs.

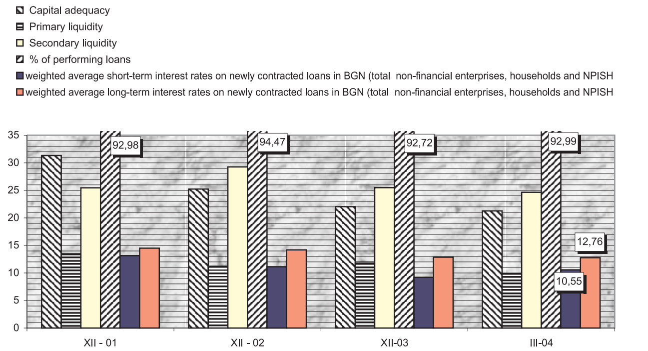
The ownership and management of water infrastructure is foreseen to be the subject of a separate piece of legislation – the Ownership and Management of Water Facilities and Systems Act which should be consistent with the Water Act and the Regulation of Water Services Act.

The strategy puts special emphasis on sources of funding and the maintenance of water systems and the terms and conditions to provide good-quality services to water consumers. Current costs of water services provision to consumers will be covered in full from individual charges paid by consumers of such services - citizens and businesses. The mechanisms to collect charges from water consumers will undergo the following changes:

- all water consumers and/or water environment users which hold permits issued as per the Water Act will pay a fee for consuming water or using the water environment and/or a pollution charge by means of which the state will cover its water management costs and will finance the management of mineral Water which are exclusively state property, the construction, maintenance and operation of the National Water Monitoring System;
- persons to whom water services are provided will pay the price of the water service related to water conveyance thus adhering to the principle of full return of costs for water services;
- prices will be regulated by the Water Services Regulation Commission depending on the line of policy of the respective ministries and municipal councils;
- pollution charges for the discharge of waste water will be levied based on pollutant substances calculated as the annual pollution load and will be linked to the issuance of permits to release waste water.

The financial sector and financial mediation in Bulgaria are dominated by the banking system. Since the beginning of the year the credit expansion continues practically without slowing down its pace, but the condition of banks remains stable, with excellent ratios of capital adequacy and liquidity and well functioning banking supervision. It is possible with regard to credit growth in the months to come that the first larger effects occur from the restrictive measures of supervision and the government undertaken or announced for a year now. 35 banks operate on the territory of Bulgaria, out of which 29 are the banks licensed to conduct transactions in the country and abroad and 6 are branches of foreign banks.

Figure 7. Selected ratios of the banking system (%).



Source: According to BNB data, monthly information bulletins

Banking system statistics

The International Accounting Standards were adopted for commercial banks in Bulgaria as of 1 January 2003 which required a change in the format and structure of financial statements. As of April 2003 the Banking Supervision Department of BNB applies **a new grouping of commercial banks** (again, with the explicit clarification that the grouping does not contain any elements of rating and should not be interpreted as an assessment of the financial condition of banks). The place of banks in the groups depends on the amount of their assets. Group I always consists of 10 banks, Group II – of the remaining ones, and Group III comprises branches of foreign banks.

According to BNB data, as of the end of May the banking system possessed assets of a total value of BGN 19 229 222 thousand, while at the end of 2003 these were of a value BGN 17 323 643 thousand (i.e. an increase of BGN 1 905 579 thousand for the first five months of the year). As of the end of May deposits totaled BGN 14 914 854 thousand compared to the end of last year when their amount was BGN 13 593 516 thousand (an increase of BGN 1 321 338 thousand for the first five months of the year). As of May the banking system profit amounted to BGN 169 150 thousand. According to BNB data the total capital adequacy of commercial banks at the end of the first quarter of 2004 was 21.28 per cent (Group III excluded) while this ratio was 22.03 per cent at the end of last year (and 25.22 and 31.32 per cent at the end of 2002 and 2001, respectively). As of the end of March 2004 primary liquidity as a total for the banking system was 9.87 per cent, and secondary liquidity was 24.64 per cent (the respective ratios three months earlier amounted to 11.98 and 25.48 per cent, at the end of 2002 – 11.2 and 29.25 per cent, respectively, and at the end of 2001 – 13.47 and 25.47 per cent, respectively). These ratios are illustrated in Figure 7.

Thus, the banking system as a whole continued to increase its assets, deposits and net current profit. The growth rate of assets and deposits for the first five months of 2004 exceeds considerably the one for the first five months of 2003. Compared to December of the previous year, these rates are respectively 11 per cent growth rate of assets by May 2004 (vs. 1.34 per cent for the same period of 2003) and 9.72 per cent growth rate of deposits by May 2004 (vs. 0.48 per cent for the same period of 2003). **The growth rate of the deposit base and the growth rate of assets are a factor and an indicator of a harder slowing down of the credit growth rate.** The net current profit of the banking system as of the end of May 2004 however was lower than the one as of the same month of last year.[32] The ratio net interest income/other non-interest income goes up in the current year (following the values of 2.30, 2.25 and 2.21 respectively in 2001, 2002 and 2003, at the end of May 2004 it is already 2.50). This reconfirms that lending remains a primary source of revenues for banks in Bulgaria. On the one hand, this reflects banks' strive to make use of the opportunities offered by the more favourable economic environment and the increased demand for loans by businesses and citizens. On the other hand, however, this suggests underdevelopment or inadequate diversification. Ratios of capital adequacy and liquidity at the end of the first quarter are lower than those at the end of 2003, and yet, these are relatively high and prove the stability of the system. This reconfirms the conclusion that **stability is in place in the banking system of Bulgaria but there are underused opportunities for development and enhancing its efficiency.**

A similar example is indirectly confirmed also when comparing the size and credit exposure of banks in Bulgaria to other countries in transition. Despite the growth over the last years **Bulgaria is still lagging behind most of the countries of Central and Eastern Europe**, and in addition, the region as a whole is still far behind the indicators of developed market economies (Table 15). This is a sign that **the Bulgarian banking system has a significant growth potential, including through credit expansion despite the current disputes around the optimal rate of such expansion.** As of the end of 2003 the net loans

32 In the beginning of 2003 a large reintegration of provisions was conducted in relation to the adoption of the International Accounting Standards, i.e. the real growth rate of income in the beginning of last year was lower.

of the banking system to non-financial institutions and other customers amount to hardly 26.2 per cent of GDP for 2003 at current prices.

Table 15. Banking assets and lending in Central and Eastern Europe, % of GDP (end of 2003)

Country	Assets	Loans
Bulgaria	50	26
Poland	65	31
Romania	33	18
Slovakia	83	34
Slovenia	89	42
Унгария	79	39
Croatia	105	61
Czech Republic	107	35
Average* For the 8 CEEC	74	34
Average* For the Euro area countries	201	102

* Non-weighted

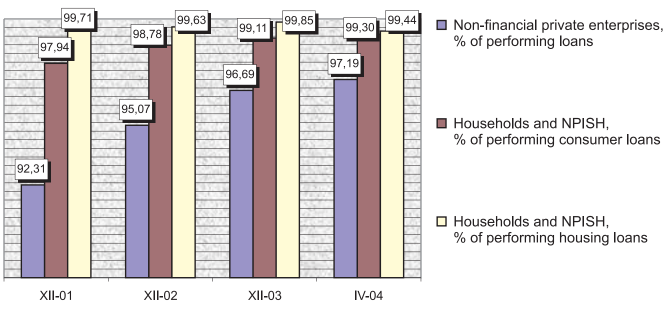
Source: Bank Austria Creditanstalt, Banking in CEE, April 2004.

Domestic credit continues to grow (under the currency board arrangements the loans from commercial banks to the non-government sector are worth monitoring – non-financial state-owned enterprises, non-financial private enterprises, non-banking financial enterprises, households and other according to the sector classification). From BGN 4 374 627 thousand at the end of 2001, receivables from loans to the non-government sector reached BGN 6 250 741 thousand at the end of December 2002. As of the end of December 2003 receivables on loans to the non-government sector already amount to BGN 9 199 919 thousand, and as of April 2004 – BGN 10 518 659 thousand[33].

The credit expansion over the last year registers **an annual growth of newly contracted loans from commercial banks of 38 per cent** (from BGN 5 189.7 m in 2002 to BGN 7 159.96 m in 2003). During the first five months of 2004 newly contracted loans reach BGN 3 586.81 m versus BGN 2 420.59 m and BGN 1 877.3 m newly contracted loans for the respective periods of 2003 and 2002. These data indicate that the first months of 2004 did not record a decline of newly contracted loans either in absolute terms or in the growth rate per annual basis (for the first five months of 2003 newly contracted loans grew by 28.94 per cent compared to the same period of the previous year, while for the first five months of 2004 this growth is 48.18 per cent compared to the same period of the previous year. **The conclusion is that for the current being the new measures of the government and banking supervision (discussed below) to restrict credit growth do not have the desired effect. However, it is possible that in the months to come this effect may occur since some of the measures are quite recent and others are only announced.**

The loan portfolio condition remains good – if 92.72 per cent of all categories of loans from the banking system are classified as performing at the end of 2003 (versus 94.47 per cent at the end of 2002), at the end of March 2004 92.99 per cent are performing loans (Figure 7). The general conclusion about the loan portfolio condition applies also to the receivables on loans from private non-financial enterprises, households and NPISH - there the percentage of performing loans goes up or remains high during the first months of 2004, too (Figure 8).

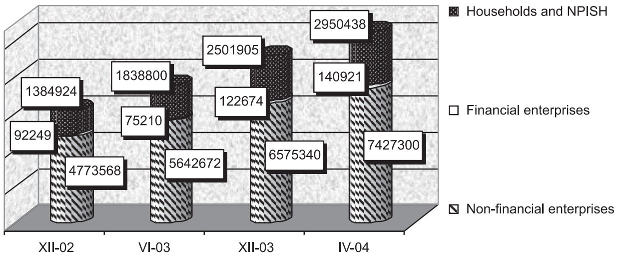
Figure 8. Loan portfolio condition



Source: BNB data and own calculations

Interest rates on short-term newly contracted loans in BGN in March 2004 are higher than those in the last month of 2003 while interest rates on long-term loans in BGN remain at approximately the same levels like three months earlier (Figure 7 again). Lending dynamics reveals additional interesting trends (according to currency, term and borrowers). Thus, for instance, the review of receivables on loans to the non-government sector from the beginning of the year shows highest absolute growth to non-financial private enterprises, but the long-term trend indicates a growth of the relative share in the total receivables on loans to households and to NPISH (from 21.35 per cent at the end of 2001 to already 28.05 per cent at the end of April 2004, Figure 9).

Figure 9. Receivables on loans to the non-government sector (BGN thousand)

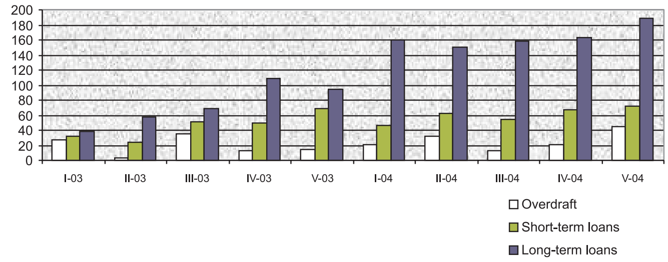


Source: BNB data, monthly information bulletins

33 It is important to note that as of the beginning of 2004, BNB, as a part of the process of harmonization of monetary statistics with the requirements of the European Central Bank, made some modifications in the presentation of monetary statistics through the monetary report. As of February, ESA'95 sector classification is fully applied (for example, the introduction of NPISH) which required reconstruction and revision of a part of the time series.

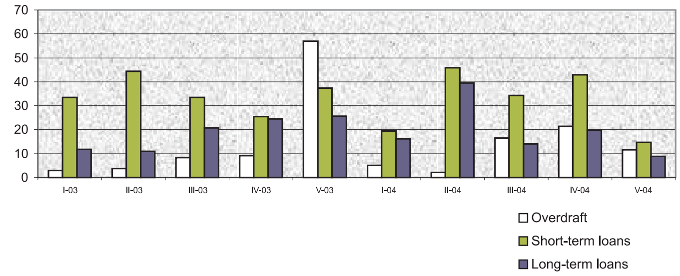
Figures 10, 11 and 12 illustrate the dynamics of newly contracted loans for the first five months of 2003 and 2004. As indicated above, the first five months of the year show increased lending activity compared to the same period of 2003. Concerning the terms and currency as a whole, **the trend is preserved of a simultaneous higher share and higher growth of long-term versus short-term loans in BGN and EUR.** With USD loans, however, there is a certain decline of both short-term and long-term newly contracted loans compared to the same period of last year. Over both periods, however, short-term newly contracted loans have a higher share among USD loans. Overall (total short-term and long-term loans) compared to the same period of last year, the decrease of the volume of contracted loans in USD versus the increase of BGN and EUR loans is probably a demonstration not that much of interest rate dynamics and interest rate levels than of the increased investment activity in the country taking into consideration the currency risk. Expectations about the dynamics of the exchange rate of USD versus EUR seem to be contradictory and in this sense – neutral towards the choice of currency when borrowing. The availability of currency risk with USD loans, however, (with EUR as a reserve currency under the currency board arrangements) predetermines the preferences to loans in BGN and EUR, especially with regard to longer-term loans.

Figure 11. Newly contracted loans from commercial banks in EUR (BGN m)



Source: BNB data, monthly information bulletins

Figure 12. Newly contracted loans from commercial banks in USD(BGN m)



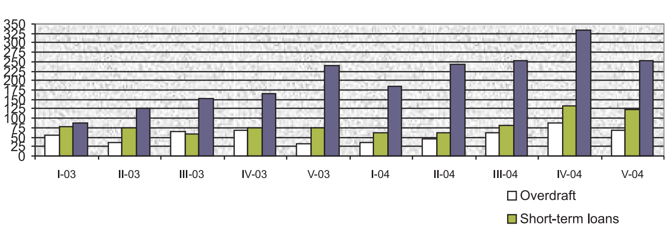
Source: BNB data, monthly information bulletins

Table 16. Changes in the structure of some assets and liabilities

	Dec-01		Dec-02		Dec-03		April-04	
	BGN thousand	% of total assets/ liabilities	BGN thousand	% of total assets/ liabilities	BGN thousand	% of total assets/ liabilities	BGN thousand	% of total assets/ liabilities
Assets	9995321	100.00	11533708	100.00	13705432	100.00	14777635	100.00
Net foreign assets	3968500	39.70	2909504	25.23	1504314	10.98	1357279	9.18
Liabilities	9995321	100.00	11533708	100.00	13705432	100.00	14777635	100.00
Deposits with contracted maturity up to 2 years	4423218	44.25	4926377	42.71	5430159	39.62	6006755	40.65
Deposits redeemable at notice up to 3 months	1232095	12.33	1375995	11.93	1619867	11.82	1738545	11.76
Debt securities issued up to 2 years	-	-	3075	0.03	2335	0.02	2408	0.02
Deposits with agreed maturity over 2 years	14689	0.15	93561	0.81	201740	1.47	278471	1.88
Deposits redeemable at notice over 3 months	-	-	-	-	-	-	40	0.00
Issued debt securities of over 2 years	6341	0.06	15962	0.14	53981	0.39	126841	0.86

Source: BNB data, analytical reporting of commercial banks

Figure 10. Newly contracted loans from commercial banks in BGN (BGN m)



Source: BNB data, monthly information bulletins

The total credit growth and in particular the increased volume of long-term loans over the recent years is off-set by some changes in the structure of banking assets and liabilities. The most visible ones, according to the analytical reporting of commercial banks, are the decreased volume and share of foreign assets, as well as the increase of certain long-term assets (Table 16).

It is evident from the table that despite the enhanced desire of commercial banks to attract more long-term deposits and to issue longer-term debt securities on the local capital market, short-term deposits still preserve the most significant relative weight in the liabilities structure.

Privatization. Lending and amendments to the regulatory framework.

Via various channels like privatization, opening of representation offices, branches and newly established banks **the foreign interest in the banking system of Bulgaria is already prevailing both in the control over equity and with regard to assets under management.**

In 2003 the last large state-owned bank remained DSK Bank AD which, together with the Encouragement Bank, accounted for the last 14.2 per cent of the state interest in banking assets (the municipal interest was 2.4 per cent[34]). The privatization transaction of DSK Bank was finalized in the autumn of 2003.

Thus, **the end of bank privatization in Bulgaria** was officially declared. **Following the sale of DSK Bank now over 97 per cent of the total assets of the banking system are privately owned[35]**. Encouragement Bank AD and Municipal Bank AD remain the last banks with state, or respectively municipal, control over the capital.

The discussion continues on the possible **threats ensuing from the increased lending activity of the banks.** The quality of loan portfolios and potential stability of the banking system stepped back as a major topic in this discussion (mainly after the subsequent IMF mission to our country in the autumn of 2003) to make room to the questions about the link between the growth of imports, and respectively of the current account deficit, and the credit expansion. IMF representatives were extremely insistent when arguing on the need to restrict the lending activity of banks and their arguments were actually accepted by BNB and the government.

Despite the prevailing understanding of the benefits of credit growth for the overall economic growth and the lack of immediate threats to the stability of the banking system, BNB in particular started to announce and undertake a series of measures to slow down the growth of lending to private businesses and households. These measures comprised first of all the **amendment of Ordinance N 9 of BNB** (Ordinance N 9 on the assessment and classification of risk exposures of banks and setting provisions for impairment losses) of August 2003. The amendment shortened by two months the period after which a credit exposure starts to be considered doubtful (with accumulated overdue payments from 91 to 120 days) or considered a loss (with accumulated overdue payments above 120 days). In the beginning of 2004 Ordinance N 9 was amended once again[36], and risk exposures of banks are now classified in four instead of five classification groups (the former groups of “doubtful” and “loss” are combined in “non-performing” with overdue payment of 90 days and above).

The fourth IMF report on the review of the stand-by agreement for Bulgaria of February 2004 points to three more **steps of the Bulgarian authorities directed towards restriction of the credit expansion.** First, this is the postponed plan of BNB to reduce the minimum required reserves of banks. Second, this is the stated intent of the government[37] to return deposited funds (of the mid of 2003) from the fiscal reserve to commercial banks with expiry of deposits maturity and even earlier. The government undertook also not to repeat similar transactions in 2004 again based on the argument that moving a part of the fiscal reserve to commercial banks creates conditions for additional credit expansion of banks. Third, BNB confirmed its support to the joint project with the Association of Commercial Banks to launch by the mid of 2004 the operation of the single credit register, that should cover also loans under BGN 10 000 (the current minimum amount of loans - separately and jointly to individual borrowers and related parties – for which BNB keeps a credit register). Registration of all loans is supposed to cut down considerably the costs of banks for evaluation of creditworthiness, for monitoring of the loan portfolio, and generally – for risk management.

To this end, in April 2004 **Ordinance N 22 on the Central Credit Register of Banks was amended.** The amendments became effective as of 1 July 2004.

Other important regulatory amendments from the first months of 2004, all of them again focused on limiting the credit growth of banks, are the following:
First, **amendments were passed to Ordinance N 8 on the capital adequacy of banks[38]** introducing additional requirements to include retained earnings of past years and the current profit in the capital base.

Thus, **the amendments to Ordinance N 7 on the large exposures of banks** generally aimed again to enhance and improve supervision over banks’ lending in specific relation to the limitation on their large exposures. **The amendments to Ordinance N 21 on the required minimum reserves to be maintained by the banks with BNB** became effective in June. The deposit base on which the amount of reserves was calculated was expanded to include deposits and debt instruments of contracted period over 2 years. For these, in particular, banks shall maintain reserves at the amount of 4 per cent.[39]

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34 Calculations were made according to assets at the end of 2002.

35 Calculated according to the assets at the end of 2003, the share of private banks in the assets of the banking system is 97.52 per cent.

36 Amendments became effective as of 1 April 2004.

37 Additional memorandum to the economic policy of BNB and the government, 15 January, 2004.

38 Effective as of 1 June 2004

39 Rumours were spreading around in June that this percentage would be raised to 8 % in the fall if the credit growth does not slow down its rate.

In the beginning of 2004 the Bulgarian authorities expressed before IMF[40] **the expectations that the real annual growth rate of receivables from the non-government sector would be limited to less than 25 per cent by the end of 2004.** In the middle of the year IMF expressed similar forecasts – **25.9 per cent** nominal annual growth rate of receivables from the non-government sector at the end of 2004[41].

40 Additional memorandum to the economic policy of BNB and the government, 15 January 2004.

41 Source: IMF, Public Information Notice No. 04/65, 18 June 2004

During the first months of 2004 the capital market in Bulgaria preserved some of the positive trends characteristic of the whole previous year. Stock exchange trading outside the privatization market continued to be active, and on an annual basis, the first months of the year marked a significant growth in turnover, market capitalization and in the stock exchange index. Again on an annual basis, the volume of traded securities dropped down insignificantly. However, what should be noted is the preserved values and sometimes the decline of many of the indicators compared to the end of 2003. During the first months, trading in compensatory instruments and investment vouchers was activated, mainly under the influence of privatization during public tenders.

Nevertheless, the role of the capital market for the financial sector in Bulgaria remains insignificant – at the end of May 2004 the total market capitalization of the Bulgarian Stock Exchange – Sofia AD was 7.3 per cent of the current GDP forecast[42] for 2004.

Table 17. Market capitalization in EU Member States and Bulgaria (EUR billion)*

Euro area (12), total	4002.1
EU (15), total	6378.7
EU (25), total	6477.4
Bulgaria	1.4
Estonia	3.5
Cyprus	4
Latvia	1
Lithuania	4.9
Malta	1.8
Poland	33.5
Slovakia	2.8
Slovenia	6.8
Hungary	16.4
Czech Republic	24

* Data for Bulgaria are as of the end of May, and for the other countries – as of the end of April, 2004

Source: Eurostat, Bulgarian Stock Exchange – Sofia AD.

The capital market remains unpopular as a channel of financial intermediation in Bulgaria. This conclusion remains valid in the comparison with the newly acceded EU Member States. In absolute terms the Bulgarian market capitalization lags considerably behind (only Latvia has lower value, Table 17). The current condition of the capital market may not be explained so much with the immediate prospects of the Bulgarian economy as a whole, but rather with the circumstance that mechanisms of financing via such an alternative non-banking environment remain unknown or non-preferred even with the availability of good investment projects. Stock exchange liquidity is going up, but overall remains low, market incentives are still not adequate for the establishment of good practices of corporate governance even in some public companies. Investment alternatives remain limited and financial intermediation is still provided mainly through the banking sector.

Stock exchange trading (excluding the privatization market and excluding the market of compensatory instruments and investment vouchers)

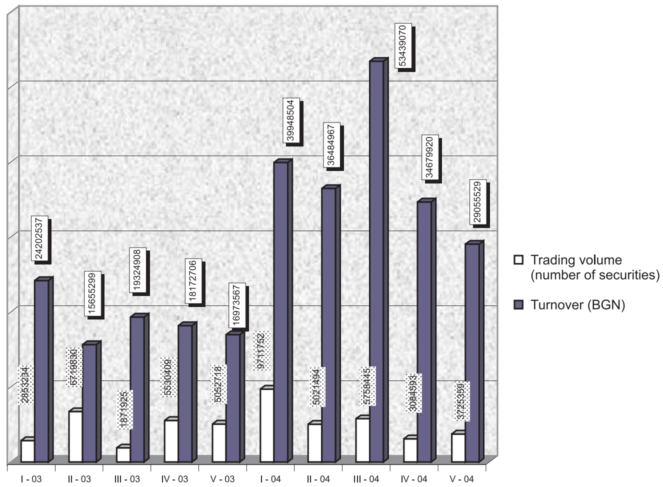
As of the end of May 2004, the market capitalization according to stock exchange data totals BGN 2 766 454 246 (out of which BGN 862 668 160 on the Official market) while at the end of 2003 market capitalization amounted to BGN 2 722 008 207 (of which BGN 985 984 573 on the Official market). **Turnover** during the first five months of 2004 totals BGN 193 607 990 with 17 589 891 traded securities. This turnover and **trading volume** does not cover the privatization market (e.g. the sale of the residual state-owned shares of Petrol AD and Lukoil Neftochim Burgas AD), nor the stock exchange traded rights, compensatory instruments and investment vouchers. However, the turnover and volume are inclusive of the block transactions (again excluding compensatory instruments and investment vouchers). This represents an increase of turnover by 105 per cent compared to the same period of last year. The trading volume, however, again on an annual basis, drops down by 20 per cent. The comparison of turnover and volume dynamics confirms the conclusion that liquidity is still concentrated on a small number of issues but can also be explained with the higher prices of traded securities. In fact, the SOFIX was rising on an annual basis (from 243.60 at the end of May 2003 to 497.00 at the end of May 2004) reaching on 18 May 2004 its highest historic value – 500.30[43].

Development over the first months of 2003 and 2004 in the turnover and volumes of trade on the stock exchange is illustrated in Figure 13. The market capitalization for one year grew by 78 per cent (Figure 14).

42 According to assessments of AEAF, Macro-economic Forecast for the Development of Bulgaria, June 2004

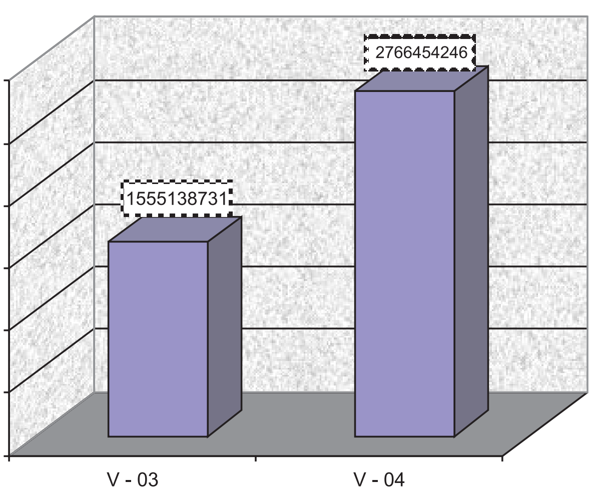
43 Followed by an insignificant decline, but at the end of June the index surpassed again the level of 500 points and reached new record values.

Figure 13. Trading on the Bulgarian Stock Exchange – Sofia AD (first five months of 2003 and 2004, excl. privatization market, rights, compensatory instruments and investment vouchers)



Source: According to data from the Bulgarian Stock Exchange – Sofia AD, monthly bulletins

Figure 14. Total market capitalization of the markets of the Bulgarian Stock Exchange – Sofia AD at the end of the period (BGN)



Source: According to data from the Bulgarian Stock Exchange – Sofia AD, monthly bulletins

Thus, the first months of the year registered positive development of the major indicators characterizing the condition of the capital market in Bulgaria (condition, understood and measured traditionally through the indicators of the Bulgarian Stock Exchange – Sofia AD). Yet, this conclusion is more categorical in the comparison to the same period of last year, than to the last months of 2003. Excluding privatization, rights, compensatory instruments and investment vouchers, but including block transactions, during the first months of 2004 the average monthly stock exchange turnover and volume of trade dropped down versus the average monthly values of the last quarter of 2003 (volume and turnover as a monthly average decline even when adding the results of the privatization market). Market capitalization and the SOFIX as of the end of May exceeded the respective values of the end of 2003 (total capitalization – by 1.6 per cent, and the index – by 9.4 per cent).

Low liquidity remains among the major problems despite the establishment of positive trends over the last year. The number of issues registered for trading continues to be high but liquid ones are little in number (these are most of the securities included in SOFIX plus some of the former privatization funds).

During the first months of the year public companies reports provoked the interest again – for the last quarter of 2003, for the whole 2003, and for the first quarter of 2004. The impression was confirmed that market actors need to and already do follow the fundamental factors influencing stock prices (in particular, the financial information from the statements and the news around the traded companies). Stock prices dynamics, particularly with liquid issues increasingly reflects corporate events which is a sign of improved investment culture of market actors and higher efficiency of the market as a whole. Unlike prior periods, most of the companies submitted their financial reports in time which to a certain extent results from the raising awareness of the importance of good corporate governance to the benefit of minority shareholders and potential investors, and hence – for the improvement of its practices in public companies.

Over the first months of the year the activity on the **bonds market** of the Bulgarian Stock Exchange – Sofia AD was within its usual limits. Overall, by the end of May 172 transactions with corporate bonds were concluded with a total turnover of over BGN 21 m on the Official market of the Bulgarian Stock Exchange – Sofia AD. On the Unofficial market a total of 139 transactions were concluded for the five months with a total turnover of over BGN 28 m.

This presents a certain activation compared to the last months of 2003, at least with regard to the number of transactions. During the period from January to the end of May 2004, admitted for secondary trading on the stock exchange were issues of corporate bonds of Raiffeisen Bank EAD (three year issue at the amount of USD 32.104 m), TBI Credit EAD (three year issue at the amount of BGN 8 m), and of Petrol AD (five year issue at the amount of BGN 15 m).

All the three issues were previously privately offered and completely sold. Private placement and subsequent registration on the stock exchange are the preferred strategy of issuers aimed at reducing the risk of placement failures and ensuring higher liquidity for the investors. Among bond issues, rather popular remain bank mortgage bonds, which reflects the increasing share of mortgage loans in banking assets.

In May 2004 the shares of one more **open-end investment company** were accepted for trading on the stock exchange – *Advance Invest AD*. Thus, the open-end investment companies traded on the Bulgarian Stock Exchange Sofia AD became four. Adding *Kapman Capital AD,* recently licensed by the Financial Supervision Commission, now five open-end investment companies and two closed-end ones (not counting *Pioneer Investment Management SA registered* in Luxemburg) operate in Bulgaria. In addition, in the first months of the year registered for trading on the stock exchange were the first **special investment purpose companies** –*TBI - BAC Real Estate Investment Trust* and *Capital Direct-1 Investment Trust*. Emergence of such companies is motivated by the prospects for both attracting the free capital available outside the banks and for its investing with increasingly better return opportunities offered by the Bulgarian capital (and generally financial) market.

Parallel to the spreading of these new schemes of collective investment, the interest is growing towards management of the investment portfolios of institutional and professional investors. New **managing companies** emerge on the market. In March FSC issued two more licenses for such companies – *UBB Asset Management EAD* (owned by the United Bulgarian Bank) and *PFBK Asset Management AD* (owned by First Financial Brokerage House).

Trade in compensatory instruments and investment vouchers, stock exchange privatization

The trade in **compensatory** instruments on the Bulgarian Stock Exchange – Sofia AD, following its launch in 2002, remains among the leading events in the area of the capital market throughout 2003. The interest towards trading in compensatory instruments is comparable to that of stock trading, though compensatory instruments prices have remained below one fourth of their par value for over a year now. However, as much as this interest is directly dependent on the progress of stock exchange privatization (especially the sale of larger blocks of shares of more attractive companies) where payment is to be effected in compensatory instruments, there is a potential to expect price rises and even higher activation of compensatory instruments trading.

An amendment to the Act on Transactions with Compensatory Instruments of 2003 allowed the Bulgarian Stock Exchange – Sofia AD to technically implement (upon assignment of a contract by the Privatization Agency) the centralized **public tenders** for the sale of stocks of joint-stock companies held by the state and municipalities, as well as public tenders for the sale of shares in limited liability companies owned by the state and municipalities. This new possibility was mainly related to the privatization of non-public companies but it indirectly raised the interest to the markets of the Bulgarian Stock Exchange – Sofia AD, too. This amendment confirmed the positive assessment and confidence in the systems of trading and settling of deals available already on the capital market in Bulgaria.

Since the beginning of the year, certain activation has been observed in the trading in compensatory instruments and investment vouchers. The statistics of compensatory instruments and vouchers trading for the period January – May 2004 show the following: a total of 19 899 deals with compensatory instruments were made with a turnover of BGN 51 071 872. The average monthly turnover for the period was BGN 10 214 374 (versus BGN 5 422 472 only in the last quarter of 2003). These data include both compensatory instruments and investment vouchers. In addition, block transactions with compensatory instruments and investment vouchers were registered on the stock exchange – 55 transactions with a total turnover of BGN 18 970 647; this represents an increase of the average monthly turnover also with block trading in non-cash payment instruments (from BGN 990 955 in October – December 2003 to BGN 3 794 129 in January – May 2004). Compensatory instruments during the first months of the year were traded in the range from 20.76 to 25.50 per cent of the par value. Prices followed a general upward trend but after the peak in March a temporary decline followed. At the end of the period under review prices of compensatory instruments started to rise slightly under the impact of the positive news around the closing of the privatization deal of BTC EAD and, respectively, the expectations for realization of the planned sale of the residual 20 per cent of the company capital against compensatory instruments on the stock exchange.

At the end of 2003 for the first time on the Bulgarian Stock Exchange – Sofia AD trading in **investment vouchers** started. In November, the Board of Directors of the stock exchange adopted amendments to the rules of trading (in particular, amendments to Appendix N 6 where investment vouchers were added to compensatory instruments). Following the FSC approval of these amendments, in the second half of November 134 132 876 investment vouchers of par value BGN 1 were registered on the stock exchange. The first stock exchange transactions in this instrument were concluded on 24 November 2003. Initially the interest was great and deals were concluded at about 17 per cent of the par value, but this was followed by a decline. In 2003 the stock exchange trading in investment vouchers reached the price bottom at 13.05 per cent of the par value but in the first months of 2004 the price of investment vouchers went significantly up. From January to May vouchers were traded at 14.01 to 23.98 per cent of the par value. Here again, like with compensatory instruments, there was a general upward trend but average prices were kept and even dropped slightly at the end of the period. Price peaks were achieved in February – March.

Although at a certain point in time investment vouchers prices became almost even with those of compensatory instruments, the difference was still preserved. The basic reason for the lower prices of vouchers than those of compensatory instruments lies in their more limited application in privatization, as well as in the fact that their validity expired in the mid of 2004[44]. With the purpose of expanding the possibilities of investment vouchers realization, in January 2004 the Privatization Agency and the stock exchange started for the first time to practically use the trading system of the Bulgarian Stock Exchange – Sofia AD[45] for the holding of the first two tenders for sale of stocks and shares in which investment vouchers could be used for the payment. Stocks from 432 companies were offered at one of the tenders (stock exchange segment “Centralized public tender”), and at the other – shares of 86 companies (stock exchange segment “Non-attendance public tender”). In addition to investment vouchers, cash and compensatory instruments could be used for payment at these tenders.

The centralized tender in the beginning of 2003 was the third one since the beginning of 2003 (i.e. from the so-called third wave of voucher privatization), but the first one organized through the trading and settlement system of the stock exchange. The non-attendance public tender (i.e. sale of shares in limited liability companies owned by the state and municipalities) was the first one in the “third wave of voucher privatization”. In June 2004 the sixth in sequence centralized public tender and the fourth non-attendance public tender were announced. Throughout the period the price of non-cash payment instruments (compensatory instruments and investment vouchers) on the secondary market was decisively influenced by the supply at the respective public tenders.

Among the major events of the stock exchange cash-privatization segment was the public offering of **residual state-owned blocks of shares of Petrol AD** (1.89 per cent of company’s capital) **and of Lukoil Neftochim - Burgas AD** (1.33 per cent of company’s capital). At the time of the sales investors’ interest resulted in parallel rise of stock prices on the “normal” market for secondary trading of the respective securities. In this way not only participants in the privatization but also speculators on the secondary market realized profits.

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44 An amendment was adopted in June to the Privatization and Post-privatization Control Act according to which the period of vouchers’ validity was extended to 30 June 2005. The decision to extend the period was made at the last moment, after the price of vouchers had registered a decline. On the other hand, it is namely the extension of the period that raised the importance of the other factor affecting the price of investment vouchers – the possibility to use them as a means of payment in the privatization at public tenders organized by the BSE. However, so far the privatization of attractive stocks and shares against investment vouchers has been fairly limited.

45 This was made possible since at the end of October 2003 the Board of Directors of the stock exchange adopted the new Appendix N 8 to the rules, which stipulates the procedures for execution of the so-called non-attendance public tenders for the sale of shares of limited liability companies owned by the state and municipalities. Again with the purpose of holding tenders assigned with a contract by PA but for the sale of stocks in joint-stock state-owned and municipal companies, at the beginning of October the Board of Directors of the stock exchange adopted the new Appendix N 9 to the rules, which stipulates the procedures for the so-called centralized public tenders.

Government Policy, Restructuring and Privatization

The Energy Act was passed at the end of 2003 and **the Energy Efficiency Act took effect since March 2004. Thereby the process of creating the basic regulatory framework of the sector was completed.** The passed version of the act specifies the Energy Efficiency Management activities and the issues related to the operation of the Energy Efficiency fund[46]. The drop out of the incentives for energy efficiency improvement activities envisaged in the first version of the act is unfavorable. The only measure preserved in the final version is the option for electricity, heat and natural gas consumers in condominium buildings who have founded associations under the EA to apply for finance from the fund. Despite that, creating conditions for private initiative in the provision of energy efficient services by way of guaranteed result agreements will help to lower the energy consumption of households and the business and will stimulate the development of the energy efficient services market.

The Ordinance on the Regulation of Electricity Prices is a bylaw to the Energy Act passed in the beginning of the year. The need to adopt this ordinance was dictated by the time limit set for approval of the bylaws and by its importance for the EDC privatization process. It lays down the specific conditions and methods at which the new EDC owners shall determine the prices of the electricity they sell and hence the amount of the profit they will be able to realize.

The basic new point in the ordinance is the price regulation method. Unlike the old procedure which was based on determining a cost ceiling, the new method is focused on the proceeds of the energy companies. This is a necessary change because the cost ceiling regulation does not create incentives for investments to improve the operations efficiency of the companies in the sector. On one hand the regulator determined the electricity sale prices and on the other hand that was done on the basis of the expenditures incurred by the energy companies. Thereby, operating on a market with almost unchangeable volume of electricity sales, the energy companies had limited opportunities to generate higher profit by cutting their limit costs. The new method eliminates this defect.

The ordinance establishes the regulation by incentives methods – “Upper limit of prices” and “Upper limit of proceeds” – which will be applied for the EDCs from the beginning of 2005 till the end of 2007. With this method the electricity price will be determined on the basis of the necessary annual proceeds from the license. All other energy companies will choose between the two regulatory methods. The regulatory period shall be from two to five years. With the incentives methods the price or the necessary proceeds are determined for the first regulatory period. In the next periods these are adjusted positively by the inflation index and negatively by a coefficient reflecting the improved efficiency of the energy company. The difference between estimated and real service quality indicators is employed to adjust the price in the “Upper limit of proceeds” method.

The effect of the positive inflation index included in pricing is not clear. The objective of this index is probably to keep unchanged the real proceeds of energy companies. At the same time, costs of enterprises might change at a different pace compared to the inflation index. This pricing method can also generate a negative multiplicative effect. Increasing the electricity price by the inflation index will probably result in higher prices of many goods and services, because electricity is a cost component in their production. This will lead to higher inflation index and then to new increase of the electricity price.

A positive aspect of the ordinance on the regulation of electricity prices is the opportunity to determine different prices for different consumer groups. That makes possible optimized and flexible pricing based on companies’ costs of supply to different consumer groups. Economies of scale can be realized from the sale of electricity to big consumers. Very strict control by the regulator is needed in this case with a view to prevent possible cross-subsidizing of the different consumer groups.

Advantageous for future private owners in the sector is the opportunity to include in the electricity price unrecoverable costs related to the transition to a competitive market and costs related to the security of supply and fulfillment of the obligations to the society.

SERC has fixed the rate of return for EDC in the first regulatory period at 16 per cent; in the next two regulatory periods it will be not less than 12 per cent. This rate can be assessed as high and acceptable to the future EDC buyers, given the low risk in this business conditioned by the secure market and the clear regulatory rules in place.

Serious activity has been observed in the preparation of **draft bylaws to the EA** in the first six months of 2004.

In addition to the regulatory framework domain, progress has also been observed in terms of the higher share of private capital in the energy sector. SERC appointed **investors for two of the eight Bulgarian gas distribution regions.** Three companies participated in the tender for construction of the gas distribution network of the Mizia region: Black Sea Technology Company AD, Plevengas EAD, Technoterm Engineering OOD. The candidates were ranked according to indicators of their financial stability, experience, investment plans and future service prices and the Black Sea Technology Company AD (BSTC) was appointed the successful bidder. BSTC AD and Technoterm Engineering participated in the tender for the Dobrudzha region. BSTC AD was appointed the successful

46 For more details see The Bulgarian Economy in the Second Quarter of 2003, Center for Economic Development, September 2003.

bidder in this tender as well. Company's investment plans for the two regions amount to BGN 164.380 m. Total network length in the two regions will be 1 212.6 km; 73 776 consumers will be connected. The gas distribution network for the Mizia region will be completed by 2013 and the network for the Dobrudzha region will be completed within 10 years after a license is granted.

In addition to the positive effect of investments on Bulgaria's macro data, the existence of a cheap alternative energy source for the consumers in the two regions will allow to cut electricity costs and consumption. Sizable economies can be realized in terms of heating in the first place. The access to a gas distribution network will result in increased investors' interest in the two regions, which will indirectly influence the employment level in a mid- and long-term perspective. The number of employed in the construction and operation of the gas distribution network (estimated at 800 to 1110 people for the two regions) will have direct effect on employment. Tender procedures have been announced for two other regions as well – Danube and Thrace.

MEER has developed an **Integrating Electricity Production Companies** draft paper. Integration will have several phases. In phase one an Electricity Consolidation Company AD (ECC) shall be incorporated. Its structure shall comprise not less than 67 per cent of the capital of Kozloduy NPP, Bobov Dol TPP, Maritza-Iztok 2 TPP, Russe-Iztok TPP, Brikel and other producers. Vertical and horizontal integration of the companies in the sector and acquisition of assets in the electricity sectors of the countries in the region are envisaged for the next two phases. Attraction of necessary funds for investments in sector development and privatization of ECC AD's subsidiaries are planned for phase four.

The need to create a structure to be competitive in a completely liberalized market in 2007 was stated as an argument for realization of the project. This need is also conditioned by the size of the competitors in the regional energy market which unite horizontally and vertically integrated companies from all businesses in the sector. The subsidiaries will remain legally independent in the newly incorporated company.

The unofficial reason for the incorporation voiced in the public space was the future privatization in the sector without the participation of the Privatization Agency.

The effects from consolidation which MEER expects are related to the opportunity for ECC to attract cheaper capital, for example by bond and security issues, for financing the implementation of energy projects. Other possible positive effects include economies of scale and more flexible privatization methods.

Creating a structure of this size generates all above mentioned positive effects, however cross-subsidizing of enterprises and activities should be prevented. For that reason and given the problems with the management of a large-scale structure, there is a need to develop detailed rules for management and control of the activities to be carried out by the company.

It should be noted that the approach underpinning the project is similar to the one applied in the restructuring of the banking sector where the results are given positive assessment.

The future of Bulgaria's **nuclear energy sector** was another major issue discussed in the public space. Major topics of public debates included the closure of units 3 and 4 of Kozloduy NPP and bringing back on the agenda the project for construction of Belene NPP.

The results of the peer review conducted by Atomic Question Group and Working Party on Nuclear Safety confirmed that all recommendations on nuclear safety have been implemented. But it was also underlined that Bulgaria must fulfill the commitments it entered into upon closing Chapter "Energy". As the technical examination was positive, the debates on the closure of units 3 and 4 remained entirely on the political level. The strong external political pressure and the possible extension of the negotiation process with the EU in the event of renegotiation of undertaken commitments were decisive for keeping the year 2006 as a deadline for closure of units 3 and 4 of Kozloduy NPP.

As regards the construction of Belene NPP, it should be taken into account that this investment project needs to be separated from the future decommissioning of the two units of Kozloduy NPP. Kozloduy NPP is an investment made in a totally different situation and for different purposes compared to the present situation and that in 2007 when a completely liberalized market will be in place. When the monopoly of NEK on the import and export of electricity is eliminated, the sale of the electricity produced will be basically dependable on the selling price. Consumers will be able to meet their needs through import as well as through purchase of electricity produced locally. This actually means that the Belene project should not be viewed as a substitute for the capacities to be decommissioned in Kozloduy NPP but as an opportunity to export.

In the decision-making process on Belene NPP the Government should be given positive assessment for its willingness and recognition of the need of wide discussions on major issues and for the active work of the Executive with the non-government sector.

The round tables, initiated by the Minister of Energy and organized jointly by MEER and the Center for Economic Development, demonstrate that. Present and former representatives of the Executive, the non-government sector, the international institutions represented in Bulgaria, the business, the academic circles, etc. took part in the discussions on the construction of Belene NPP.

Many arguments in support of Belene NPP were pointed out during the discussions[47]. Questions aimed at clarifying further the need and future efficiency of investments in new nuclear power capacities were raised.

The basic arguments “for” included: established need of new nuclear power capacities in the period 2010–2015; environment protection requirements can be fulfilled because the production of electricity by nuclear power facilities does not generate harmful emissions in the air; local resources and renewable energy sources are limited; the existing infrastructure, staff and experts in the field can be used. Another serious argument “for” was the current price of the capital necessary for the investment, manifested in the record-low interests on loans in Europe and the USA, which are expected to rise in the future. At this stage the project also meets with public approval.

The arguments “against” pointed out during the discussions included: forecasts for the future electricity needs on national and regional level are not quite accurate. A need of more accurate and precise calculation of project’s financial benefit was pointed out as well as absence of calculations of its alternative price. The need to specify the capacities of the new nuclear reactors and the precise time of their putting into operation was also highlighted.

A fundamental question related to State’s involvement in the decision-making process and in the construction of new production capacities and the alternative of leaving these decisions to the private sector was raised during the discussions.

Taking into account these issues, it should be pointed out that 100-percent accuracy of the forecasts of future consumption and development of supply on regional level is not possible and arguments “for and “against” will always be stated. There are many reasons for that; the long time horizon planned for operation of the new nuclear power facilities is of particular importance. The effect of such large-scale investments on the general economic situation of Bulgaria should also be taken into account. The agreements with different Bulgarian and foreign sub-contractors would enhance the investment activity on one part and on the other part the import of materials and technologies will have effect on Bulgaria’s import-export ratio.

The time limits for privatization of the electricity distribution companies have been extended at investors’ request. Thus the deadline for submission of final offers by the candidates was set at 25 June 2004. Five companies have been admitted to the final phase of the tender for privatization of the EDCs: ENEL – Italy, E.ON – Germany, EVN – Austria, CEZ – Czech Republic, and PPC – Greece. The time limits have been extended in relation to the analysis of the electricity distribution situation and the post-sale operational environment conducted by the candidate-buyers. Total 2003 accounting profit of EDCs amounts to about BGN 123[48] m.

Another aspect of the privatization process in the energy sector is **the sale of district heating companies and thermal power plants**. PA has chosen the sale via the stock exchange method for 14 district heating companies. In 2003 the agency tried to apply the same method in the sale of three thermal power plants. The specific activity of these energy companies and the fact that with this sale method one cannot impose additional conditions on buyers led to termination of the announced sale procedures. Consequently the Council for Economic Policy had to take a decision for sale of the energy companies intended for privatization by tenders and competitions and for appointment of advisor for the sale of the three thermal power plants. Based on the decision made, a competition for appointment of an advisor for the sale of Thermal power plant Bobov Dol EAD, TPP Varna EAD and Toplofikatsia Russe EAD was announced in May. The advisor will provide assistance to PA for implementation of the privatization transaction and shall conduct marketing for the purposes of the privatization of each one of the companies. Public tenders have been announced for the companies Pravets, Loznitsa and Brikel.

There are generally three basic conditions which will have effect on the results of heating companies’ privatization. The first one is the reported progress in terms of 2003 financial results. As a result of the price reforms and the investment activity of the heating companies the 2001 loss of BGN 82.26 m was compensated and in 2003 they realized accounting profit of BGN 9.2 m.[49] The other two factors that will have effect on the final result of the privatization are the changed regulatory framework in terms of thermal energy pricing and the phasing out of the subsidies for these companies by 2005.

The question of the simultaneous privatization of TPP Varna and TPP Bobov Dol and their future inclusion in the Electricity Consolidation Company remains open.

Energy Prices

In the first half of 2004 **international market crude oil quotations** reached record-breaking levels (Figure 15). The Brent oil price per barrel fluctuated within the broad range of USD 30 - 40. In the period January – June 2004 oil prices registered increase of over 20 per cent. This increase was accompanied by about 2 per cent appreciation of the US Dollar, which continued firm at levels of BGN 1.60 = USD 1 at the end of June. The decisive factors for crude oil prices included again the news about the geopolitical situation in the Middle East and the other oil exporting countries. The high levels of seasonal

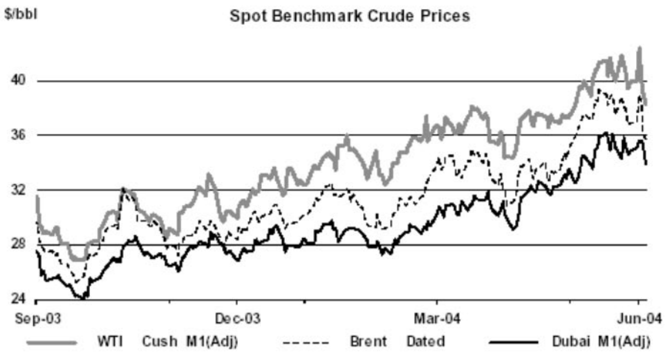
47 Round-table documents are available in Internet at: http://www.doe.bg/cgi-bin/i.pl?l=1&p=650

48 According to MEER estimates.

49 According to preliminary data from MEER.

and speculative demand were the other factors determining high oil prices. In response to these trends OPEC decided to increase the production quotas.

Figure 15. Spot Crude Oil Price Dynamics for WTI, Brent and Dubai Grades



Source: Monthly Crude Oil Price Report, International Energy Agency, June 2004, http://omrpublic.iea.org/omrarchive/10jun04pri.pdf

The situation on the international oil markets also has effect on the Bulgarian economy, because Bulgaria satisfies almost all of its needs from import under trade conditions following international market dynamics. That resulted in higher end prices of fuels on the Bulgarian market.

If international market fuel quotations continue high, that may have a negative effect on the pace of economic development in an international and national aspect.

New gas prices took effect since early July. An average increase of about 6.5 per cent against March 2004 prices has been reported. Prices for consumers connected to the gas transmission and gas distribution network registered increase to BGN 227.50/1000 cub.m. and BGN 235.22/1000 cub.m. accordingly. The increase is basically a result of the higher prices of alternative fuels and the appreciation of the US Dollar in the pricing period. This increase will have most unfavorable effect on the companies and enterprises using natural gas as basic raw material for their production.

The last planned increase of electricity and heat prices became a fact since 1 July 2004. Thereby complete cost coverage of the supply of electricity to household consumers has been achieved and a minim profit level has been guaranteed. Only the price of the monthly electricity consumption above the first 75 kWh was increased by 13.51 per cent. The higher electricity prices are not expected to result in serious drop in the purchasing power of Bulgarians in the summer months because of the seasonal decrease of the prices of many foods and the absence of heating costs. The planned 10 percent increase of the heat prices combined with the higher electricity prices will have a more pronounced negative effect in the winter months.

The results achieved in the previous six months are encouraging for the future development of the sector. The fundamental legislative framework has been completed with the adoption of Amendments to the Roads Act, Amendments to the Civil Aviation Act and Act on the Marine Spaces, Inland Waterways and Ports of the Republic of Bulgaria. Thereby the foundations for development of competition and penetration of private capital in the road transport, port and airport services have been laid. Some development has also been observed in terms of the privatization processes.

The adopted **Amendments to the Roads Act** regulates the penetration of private capital in the construction, repair and maintenance of the road transport network[50]. The concession on republican roads or parts thereof is a public-private partnership method aiming at improving the quality of the national road infrastructure. The Act provides for a possibility to release the concessionaire from paying concession charges for certain time limit or for the whole concession period. The Council of Ministers takes this decision depending on project's cost efficiency, the necessary investments, the traffic level and the amount of pass charges. The possibility for concessionaires to obtain right of ownership on the proceeds from highway pass and/or use charges is another positive aspect of the act.

The introduced vignette charge is the other basic point in the Amendments to the Road Act. The positive aspects of this paid pass include more flexible cost management for the business owing to the different validity of vignettes (week, month or a year). **The Republican Road Infrastructure Fund** has been set up for the purpose of more efficient management of the funds for maintenance and repair. The proceeds from the sale of vignette stickers shall be accumulated in this fund and shall be spent only for repair and rehabilitation of the republican road network. The separation of the republican from the municipal road network and the need to pay vignette charges only for the use of the republican road network also contribute for the more efficient and purposeful utilization of the assets accumulated in the fund. Persons traveling mainly within municipalities will also feel the positive effect. Yet complications and low effect are possible in the event of mixed ownership of the road network within a settlement where it is not possible to travel avoiding the republican road sections.

The Act on the Marine Spaces, Inland Waterways and Ports of the Republic of Bulgaria was part of the regulatory framework for the sector adopted in the first months of 2004. It regulates the issues concerning the marine spaces, inland waterways and ports of the Republic of Bulgaria. The public-private partnership principles are laid down with respect to ports and port activities as well. The investment initiative option is laid down for the rehabilitation and expansion of existing ports as well as for the construction of new ports. The Act also regulates the incorporation and operation of the **National Ports Company.** The company's scope of business includes property management, organizational management, construction and reconstruction of public transport ports of national significance. The Minister of Transport manages and controls the port activity in the Republic of Bulgaria through this company. A new point in the Act is the provided access to the port services market, i.e. port operators' right to provide services in the public transport ports. Access can be provided by way of port services agreements or concession on terminals in public transport ports of national significance. The rehabilitation, reconstruction or construction of a new port terminal can be a condition for granting a port activity to a concessionaire. By analogy with the concession conditions for roads, the concessionaire can be released from the obligation to pay concession charges for certain time limit or for the whole concession period with respect to ports as well. Incentives for penetration of private investors in port activities are laid down in the Transitional and Final Provisions of the Act. The import of goods for implementation of projects for port infrastructure or survey of inland waterways and navigation conditions shall be exempt from VAT, excise duty, charges and duties in two cases – for implementation of projects with direct financing from grant aids and/or loans from international financial institutions, where the Republic of Bulgaria is a guarantor of the loan, or when the financing organization recognizes the exemption from taxes, excise duty, etc. as co-financing from the Republic of Bulgaria.

Creating conditions for public-private partnerships in the sector is a good prerequisite for competition in the port activities field. The objective is to improve the efficiency and quality of the services provided by Bulgarian ports. That will have a favorable effect on the companies in the national transport services sector as well as on all other companies engaged in foreign trade. A positive effect can also be expected in terms of increased flow of goods through the country – provided that adequate conditions are in place for competition in the handling of marine goods in a regional aspect. These effects can be expected in a mid-term and long-term perspective.

The Amendments to the Civil Aviation Act became a fact in June. The basic points in the Act concern the conditions for competition in ground-based services and the options for concessions on civil airport management and operation activities[51].

The fundamental laws have been passed and **now the necessary regulations need to be adopted.** That should be accomplished on time with a view to provide the necessary conditions for penetration and smooth operation of private companies in the different businesses in the sector.

50 For more details see The Bulgarian Economy in the Fourth Quarter of 2003, Center for Economic Development, March 2004.

51 The principles and conditions included in the draft law have been adopted. For more details see again The Bulgarian Economy in the Fourth Quarter of 2003, Center for Economic Development, March 2004.

The conditions for **competition in the railway sector** created as early as the beginning of 2002 with the Railroad Transport Act were not utilized until May 2004. The private company Bulmarket – DM OOD got licensed for carriage of goods by railway. At this stage the company will carry goods in the section (Russe-North) – (Russe – Marshalling Yard) – Kaspitchan. The license is of unlimited duration and the conditions at which it has been issued will be checked every five years.

The emerging competition in the cargo transportation sector is explainable by the fact that in this sector conditions for making profit are in place, whereas in the passenger transport sector service prices do not cover yet actual service costs. Important for the future penetration of private carriers will be the overall industrial development and foreign trade of Bulgaria as well as the charges which the Railroad Infrastructure State Company will levy for use of the existing railroad network.

Success has also been achieved with respect to the **privatization in the transport sector.** The Bulyard Consortium took possession of the assets of Varna Dockyard, having offered at the end of 2003 the highest price of USD 16.666 m for the dockyard with a commitment to invest USD 17.7 m within three years.

The sale of 29.6 per cent of the capital of Bulgarian River Shipping EAD was also realized in the first half of 2004. The sale was realized on the stock exchange for compensatory instruments – 264 654 shares were bought with instruments with total nominal value of BGN 10 909 159.

A bond issue of BDZ was placed in May for the purpose of improving the resource base. It was reported as the first of its kind issued by a state company and the selection of this financing method can be given a positive assessment. This is a six year issue with a nominal value of EUR 30 m, fixed coupon of 6 per cent and three-month repayment installments, one year grace period for repayment of the principal. The issue is guaranteed by almost 3 620 freight cars owned by BDZ. The success of this bonded debt could put the start of more flexible financing methods in the other areas with prevailing state ownership as well.

The investment activity processes have been stirred up with respect to the construction of **the second bridge over the Danube.** In May the Government approved the second tranche of EUR 20 m of the EUR 70 m loan granted by the European Investment Bank for the Dunav Most 2 Project. EUR 5 m have been utilized so far for appointment of international financial advisor on engineering and management.

By 14 June 15 companies submitted offers for participation in the tender for design and construction of Dunav Most 2. The tender will have two phases. In the fist phase a commission will make preliminary expertise. The companies admitted to the next phase will submit final offers.The bridge design and construction price will be decisive for the final selection.

Assessment of the possible financial efficiency of the construction and operation of the Vidin – Kalafat Bridge has not been made yet. The processes of higher integration of Bulgaria in the Trans-European Transport Networks and generally in the EU will probably result in intensified transit traffic through the country. Consequently there is a need to enhance the capacity of the transport infrastructure. As a part of Transport Corridor No. 4, the bridge will probably accelerate the road and railway traffic between the two banks. And while the road traffic has the ferryboat connections as an alternative, the direct railway transport has no such option. The possible construction of the bridge could support the economic development of the region by generating additional employment in the construction and operation of the facilities. The indirect effect of such facility would be the development of many activities in the services sector.

Despite that the new bridge will lie rather remote from the existing one in Russe and although they belong to different Trans-European corridors, the existence of two bridges will certainly result in division of a large portion of the transport traffic. Hence the question of ensuring maximum load of the capacity of the two bridges and the time period in which that could be achieved.

The first half of 2004 brought some very important changes in the Bulgarian telecommunications market which will certainly have effect on the development of the sector and will contribute to the improved quality and diversity of offered services. The top events are the privatization of the Bulgarian Telecommunications Company and the parallel sale of Mobiltel. At the same time, the first signals of real competition on the fixed voice services telecommunication market came from the telecommunications operators licensed last year.

It would not be too much to sum up that the first six months of 2004 passed under the sign of the privatization of BTC. After a series of scandals and pass-the-buck games between government institutions the company was finally sold to a private investor. In mid June the sale of BTC is already a fact and the buyer acquires 65 per cent of its capital for BGN 280 m. Along with that the buyer Viva Ventures obtained the third GSM operator license for BGN 54 m, but not in a tender procedure, which caused further tension and the discontent of some experts in the telecommunications business. It now remains for the long-awaited transaction to yield the desired effect for the economy and the society – modernized communication infrastructure and improved quality of services in the first place.

At the same time the first Bulgarian GSM operator Mobiltel changed some of its owners for the amount of EUR 1.2 b. The company was bought by a consortium comprising three shareholders in Mobiltel Holding (Martin Schlaff, Joseph Taus and Herbert Cordt) and 7 private financial investors (ABN AMRO Capital, Citigroup Investments Inc., Communications Venture Partners Limited, Sandler Capital Management, Innova Capital, Global Finance and 3TS Venture Partners. The transaction can be characterized as the biggest one on the Bulgarian telecommunications market; some experts call it the biggest leveraged buyout in Central and Eastern Europe. To date Mobiltel holds a share of over 76 per cent in the Bulgarian mobile telecommunications market and has more than 2.5 users, which makes it one of the top actors on the local telecommunications market.

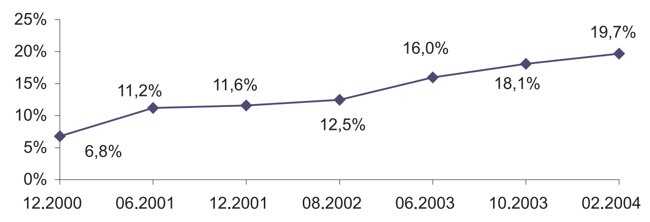
In April another telecommunications operator - Cabletel – officially announced its intentions to enter the national fixed voice telephony services and Internet market. In the beginning the services will be provided only in some regions of Sofia and Plovdiv and later they will cover other towns as well. By the end of May Cabletel has signed network interconnection agreements with Mobiltel and Globul, but not with BTC yet. The company managers send clear signals of making the operator the first real BTC competitor, which will be to the benefit of end-users. Despite that the interconnection with BTC is of paramount importance for the future of the new operator because BTC is still the mass telecom operator of Bulgaria. To date Cabletel has invested over USD 37 m and plans to invest another USD 100 m by 2006.

Along with that another new telecom operator – Netera – completed a project for building an optical network between Sofia and Rousse. The investment exceeds USD 1 m; funds come from the company and from the United Bulgarian Bank and Interlease group. A 622 Mbps high-speed optical backbone connects Bulgaria to the Rumanian telecommunication networks.

Given this accelerated development of the sector, the information presented in the analysis of the CBN - Pannoff, Stoytcheff & Co Agency, which ranks the telecommunications business among the most profitable Bulgarian businesses, is not surprising. The agency estimates the 2003 aggregate net profit at about half billion leva – about BGN 100 m higher compared to the banking sector. Subscribers of mobile operators alone will exceed 4 m people – a fact certainly accompanied by permanent growth of companies' proceeds.

The number of Internet users in Bulgaria also registers permanent growth in recent years (Figure 16). According to data from Alfa Research Agency, as of February 2004 the share of people entering the web accounts for 19.7 per cent of adult Bulgarians.

Figure 16. Internet users in Bulgaria (share of Bulgarian population at the age of 18+)



Source: Alfa Research (www.aresearch.org)

The growth of Internet users is a logical process and there are several reasons for it – the Bulgarian content on the web registers increase, alternative access sources appear and prices go down, and, last but not the least, knowledge of Internet and of the opportunities provided increases. At the same time the web expansion level is a precondition for fast growth of e-government and e-trade because it ensures adequate and growing demand of e-services.

Speaking about the development of the Bulgarian Internet market, one cannot miss the launch of BTC's ADSL (Asymmetric Digital Subscriber Line) service in February 2004. The users have long expected the real start of this service because it has considerable advantages to the ordinary dial-up – first, ADSL allows simultaneous and independent use of the phone for conversations and offers speeds of 96 Kbps to 384 Kbps. At this stage subscribers can be connected only in Sofia, Plovdiv and Varna, but with the digitalization of BTC the service will become accessible in other regions as well.

Yet the launch of the ADSL caused the discontent of the other Internet providers who cannot compete with the telecom in this access channel without access to BTC's network. This actually makes BTC a monopolist in a segment of the Internet market. In view of that the Bulgarian Internet Association deposited an official letter with the Communications Regulation Commission[52] whereby it requests the regulator to oblige BTC to provide an opportunity for submission of competitive offers for mass broadband Interned connection via ADSL. Solving this problem will further improve the Internet access conditions for users, which is important for Bulgaria's overall development.

The Regional Center of the European Software Institute (ESI Center Bulgaria, www.esicenter.bg) was officially opened in early 2004. The basic objectives of ESI Center Bulgaria include promoting the most advanced quality standards and software engineering methods (SW-CMM, CMMI, SPICE and BITS), and organizing special courses tailored to the needs of the companies in the region.

ESI Center Bulgaria was formally set up in 2003 under a joint project of the Ministry of Transport and Communications and the United Nations Development Program; project contractors are Information and Communication Technology Development Agency at MTC and BASSCOM. The Bulgarian software center is the fourth in the world and the first in Eastern Europe.

Eighteen experts from leading Bulgarian software companies got trained and certified in the first course organized by the center in April 2004. The acquired knowledge and skills will enable the certified professionals to start applying Capability Maturity Model® Integration (CMM®I) in their companies. The CMM®I certification is of paramount importance for the good positioning of the companies in the modern competitive environment of the global software market. The existence of such certification center in Bulgaria is a serious advantage for all software companies, which intend to participate in international projects, as it offers them the best global standards under conditions tailored to the local market and reality.

The final plan for implementation of Bulgaria's **Strategy on e-Government** was published in March. The strategy itself was adopted at the end of 2002 and in this sense the approved plan for its implementation comes rather late. At any rate, it contains specific actions to attain strategy's goals, which are divided in 7 basic groups: service, connectivity, information and operations environment, centralized services, e-democracy, and management. The plan further envisages connecting the administrations on all levels (central, regional and municipal) in an integrated network. It also provides for creating a national e-archive; free access via Internet to current texts of existing laws and regulations; creating an e-register of petitions; studying the opportunities to create an electronic system for elections; putting into operation an electronic public procurement system.

Adopting a plan is a mandatory step towards e-Government, but to achieve the desired results, the plan needs to be strictly complied with. The basic problem is that actions are duly described in a chronological order, but financing is not provided. To raise the funds, the Government relies less on the state budget and mostly on finance from international donors. The financing of a large portion of the projects is not clear yet. Given the limited capacity of the state to utilize funds from international projects (the PHARE execution in the high technology area is a sufficient example), one can assume that it would not be easy to secure the funds for implementation of the plan.

A special association related to Internet and Internet applications development was registered at the end of April – **the Bulgarian Web Association** (BWA, www.bwabg.org). The basic objective of BWA is to assist and protect the interests of all who do business in the area of design, preparation, organization, realization, and maintenance of Internet sites, web design and Internet advertising. The association works towards creating and establishing high professional standards and professional ethics among its members and will provide assistance for explaining new laws and regulations concerning Internet and the work in the web space. Along with that BWA will make every effort to create professional standards and popularize the global web as a means of communication and the opportunities of Internet as a national media.

The fifth **e-Readiness Report** developed on an annual basis by the Economist Intelligence Unit (EIU) was published in April too. The 2004 study covers 64 countries (4 more compared to 2003). Besides, the overall assessment contains a new criterion – broadband Internet distribution – on which most countries register very poor performance. Inclusion of new countries somewhat explains Bulgaria's drop in ranking from 40 (2003) to 42 (2004). Yet at the same time the overall assessment of the country has improved from 4.55 to 4.71 (the maximum is 10).

This year again the top places in the ranking are occupied by the Scandinavian countries – Denmark (1), Sweden (3), Norway (4) and Finland (5). The row is broken only by England, ranking second. The top countries have overall assessments above 8, which is twice that of Bulgaria. Ranking developers and report authors assess as positive development for Bulgaria the emerging software and outsourcing niche, which is also typical for India and South Africa (ranked 46 and 32 accordingly). To compare, most new EU members are ranked between 26 (Estonia) and 39 (Slovakia), and their assessments vary between 6.54 and 5.33 accordingly.

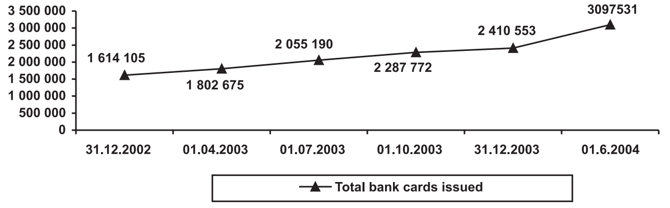
At the end of March the Council for Economic Growth approved a decision for **the set up of four clusters – one of them for information and communications technology**. The ICT

[52] http://www.bina.bg/information/pismo_adsl_menu.htm

cluster is expected to involve all companies in the ICT sector, a couple of state agencies and representatives of ministries concerned with the sector's development. The set up of such cluster could be very useful for improving the competitiveness of Bulgaria's ICT companies. The sooner the implementation of Council's decisions starts, the greater the benefit from the set up of Bulgaria's ICT cluster will be.

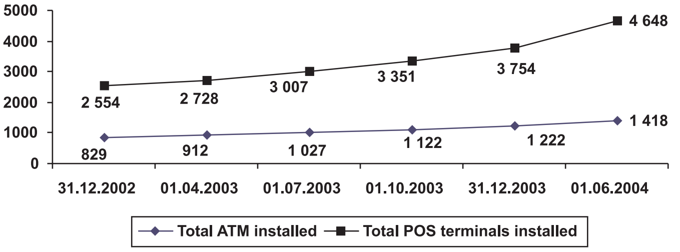
The **growth rates of the number of issued bank cards, operating ATMs and POS terminals** register continuing increase in the first half of 2004 (Figures 17 and 18). The penetration of e-payment methods facilitates transactions and is a sign of good economic development. An increasingly higher number of banks offer credit cards, which is also a proof of a stable and progressing banking sector.

Figure 17. Total bank cards issued (2002 - 2004)



Source: Borica AD (www.borica.bg)

Figure 18. Total ATM and POS terminals installed (2002–2004)



Source: Borica AD (www.borica.bg)

Number of Tourists and Revenues from Tourism

According to data from the Ministry of Economy, the number of foreign nationals who visited Bulgaria in the first quarter of 2004 totaled 621 843 people (transit passengers excluded) registering an increase of 24.5 per cent against the same period of 2003. **Foreign tourists,** i.e. foreign nationals who visited Bulgaria for holiday and vacation purposes, totaled 496 711 people, registering an increase of 25.9 per cent against the first quarter of 2003.

Greece accounts for the highest number of tourists – over 158 thousand people, registering an increase of 47.7 per cent against the first quarter of 2003. Macedonia is ranked second (44 thousand tourists), followed by Great Britain (31 thousand tourists). Great Britain registers record-breaking growth in the number of tourists (68.7 per cent). These visited mainly the big winter resorts Borovetz, Bansko and Pamporovo. The number of tourists from Israel, who basically visit Bulgaria for gambling tourism, registered significant increase. At the same time the number of tourists from Germany, who are traditional for Bulgaria, registers lower growth in the first quarter of 2004 - 13 per cent.

Bulgarian nationals, who traveled abroad in the period January – March 2004, total 787 thousand people for all types of purposes, registering an increase of 21.2 per cent against the same period of 2003. Turkey, Serbia and Montenegro, and Germany account for the highest number of visits.

The upward trend in the number of tourists continues in April and May. According to MoE's data, in the first five months of 2004 the number of foreign tourists (who visited Bulgaria for holiday and rest) registered an increase of 25.36 per cent. In the period January – May 2004 total visitors to Bulgaria (excluding transit passengers) registered an increase of 24.5 per cent against the same period of 2003. The EU (excluding the 10 new EU Member States) accounts for the highest growth in the number of tourists – 46.16 per cent, which makes EU the most significant market for Bulgaria's international tourism. Greece remains at the top accounting for the highest number of tourists; the number of tourists from Great Britain, Germany, France, Sweden, as well as from Macedonia, Serbia and Montenegro, stands high again. Tourists from Italy and Russia register increase as well.

In the first five months of 2004, Bulgarian nationals who traveled abroad totaled 1.455 m people, registering an increase of 20.2 per cent against the same period of 2003. Turkey accounts for the highest number of visits, followed by Greece, Serbia and Montenegro, Germany, and Macedonia.

In the first three months of 2004, **revenues** from international tourism totaled EUR 199.8 m registering an increase of 28.8 per cent. For the same period, Bulgarians' **spending** on trips abroad total EUR 154.9 m, registering an increase of 26 per cent. **Net revenues from tourism for the first quarter of 2004 total EUR 44.9 m.**

The above data support the definition of EU's European Commission for Tourism, which characterizes Bulgaria as the most rapidly developing tourist destination against the 2003 decline of -1.2 per cent in global tourism (Europe, however, preserved a growth of 0.4 per cent).

MoE projects a growth of 6-7 per cent in the number of foreign tourists for the summer season. Great Britain, Russia and the Scandinavian countries are expected to account for the highest growth in the number of tourists.

In the summer season MoE expects a growth of about 25 per cent in the number of **tourists from Russia** to about 150-160 thousand people. Spain and Turkey are the most significant competitors to Bulgaria on the Russian market. Bulgaria registers good demand in terms of Russian tourists, which is explainable by the fact that the country is known and there is no language barrier. Demand from Russian tourists with higher purchasing power, who prefer higher category hotels - 4 and 5 star, registers increase. Overall, the interest of Russian tourists in low-category bases and bus programs registers decline at the expense of airplane programs.

Alma Tour is a tour operator bringing tourists from Russia in Bulgaria (10 thousand tourists from Russia for 2003). Other tour operators working with tourists from Russia include Green Tour Plus, Dia Travel, etc. A major problem preventing the increase in the number of Russian tourists is the inadequate advertising of the Bulgarian tourist product. Major competitors like Turkey, Egypt, Spain, Tunisia, are ahead of Bulgaria in this respect. The visa problem with Russian tourists is more or less conquered as Bulgarian consulates are very operational and expedient. Besides, in early April the Government adopted a decision to temporary exempt from charges the visas for organized tourists from Russia, Ukraine and Byelorussia, which further facilitates the procedure.

Intensified and result-oriented measures to attract **American tourists** to Bulgaria are taken as well. The meeting of 8 American tour operators organized in May near Varna was focused on this task. The participants made a tour of Bulgaria with a view to identify the opportunities for eco, spa and rural tourism. Visits were focused on Veliko Turnovo, Arbanassi, Sofia, the Rila Monastery, Sandanski. Another 40 representatives of the American tourism business are expected to visit Bulgaria in November and to make a second tour of Bulgaria for sightseeing and identifying tourism opportunities.

In principle the Balkan region is quite attractive for American tourists, but their number in Bulgaria is small yet. American tourists have a couple of major requirements – excellent hygiene, fair treatment of customers, absolute clarity with respect to prices, and information about the additional services offered. The lack of direct flights to Bulgaria is also a barrier to the higher inflow of American tourists, but this problem may well be solved by the autumn. – negotiations with Bulgaria Air for regular Sofia – New York flights are in progress.

In the beginning of 2004, big **German tour operators** registered lower number of bookings for summer holidays in Bulgaria by German tourists. TUI also registers decline in bookings (by 8 per cent compared to 2003), ITS (by 10 per cent); Al Tours' bookings stand at last year level. Only Neckermann registers increase of 23.5 per cent. This negative change is attributable to the stagnation in the German economy and the demand of cheaper offers on the part of consumers – mostly middle class and people in the lower income brackets who are potential consumers of the Bulgarian tourist product. Hotel prices in Bulgaria's Black Sea resorts register high levels – they are above those of major competitors in the Mediterranean, including Spain, Tunisia and Morocco.

Foreign tourists are put off by serious in-resort problems as well – the question is about the construction of new projects along the Black Sea coast. This is a grave problem which might have a negative effect on the development of Bulgaria's sea tourism: construction disproportions and over-equipping big sea resorts with special infrastructure (the building density in the Black Sea resorts is above the standard rate); the beach zone cannot accommodate so many tourists (in Golden Sands, for example, the beach has a capacity of about 17 thousand people, while the resource base offers over 30 beds); permanent environmental damage and disturbed environmental balance; insufficient general infrastructure – water-supply and sewerage, roads.

There are also short-term negative effects – continuing construction works, which generate noise and dust, and unfinished streets create chaos in the resorts and put off holiday-makers. While MoE sent letters to the mayors of the Black Sea municipalities to stop construction works from 1 May till 1 October, in the big resorts construction continued till the end of May, which generated further tension. For that reason the big German tour operator TUI announced that in 2005 the summer seasons will start for them on 1 June and not on 1 May.

Alternative Tourism

Special forms of tourism – rural, eco, spa, etc., register significant progress in their development. **The National Strategy and Action Plan for Development of Eco Tourism** developed in cooperation with USAID was officially presented in early 2004. Calculations show that Bulgaria needs BGN 24.5 m to become a leading eco tourism destination. The funds are needed to: improve the information about the Bulgarian eco tourism; develop an Internet gateway for the best practices in the industry; improve road marking; build eco tourism centers; provide advisory services for small and medium-sized enterprises. Funds are also needed to train the people employed in the industry, for marketing and advertising, to strengthen the institutional capacity of municipalities, agencies, business organizations. Financing from European programs – PHARE, SAPARD; from the budget and from international financial institutions is envisaged. The Strategy covers a period of 10 years, the Action Plan to it – a period till 2008.

PHARE will provide support for Bulgarian eco tourism development projects. Funds will be used for rehabilitation and reconstruction of eco tourism-related special infrastructure and for building new tourist sites. Total budget of such projects amounts to EUR 5.3 m., including EUR 4 m from PHARE of which EUR 200 thousand for institutional building. EUR 1.3 m come from the state budget. A call for proposals in this field was announced in May.

A Strategy for Development of Rural Tourism has been developed within the OPTOUR Project. The major conclusion is that Bulgaria provides excellent opportunities for development of rural tourism – natural and cultural heritage; significant material base – small hotel-and-restaurant complexes and family hotels in regions which could attract foreign tourist. Rural tourism is an important segment of European tourism. The EU (15) has over 200 thousand suppliers of farm and rural tourist services, who provide over 2 m beds.

On the other hand, the survey conducted in connection with Strategy's development reveals that Bulgaria is not famous yet as a tourist destination in general and is even les known as a country with good opportunities for development of rural tourism. This confirms again the need to take proactive measures for national advertising.

In this respect the partnership with the Swiss Agency for development and Cooperation which supports the **Stara Planina Regional Tourism Association** is very fruitful. In 2004 it will allocate BGN 154 thousand to popularize this region. Association's work is focused on the tourism development of Middle Stara Planina, supporting local tourist associations, improving the quality of services and promoting the region. Planned activities include: developing a catalogue of houses for accommodation, hotels, restaurants and entertainment places; developing an information system model for gathering, updating and disseminating tourist information from and for the region; creating a tourist map of foot, bicycle and horse routes. A brochure promoting the resources in the rural areas of Lovech region will be published.

Investments in the Tourism Sector

Active construction work in the sea resorts continued in the first months of 2004. A national meeting of hoteliers was organized in **Sunny Beach** in early June where it was announced that by that time investments in the resort complex exceeded EUR 500 m. Ten new high category hotels will be opened in 2004 alone. The active season in the resort has started and in June alone the number of tourists totals about 30 thousand people, which means that the special infrastructure is occupied at 80 per cent.

Sozopol and Chernomorets have 50 thousand beds, including private lodgings. The central part of old Sozopol has been rehabilitated within the Beautiful Bulgaria Project Sizable investments were made in the resort village **Djuny** near Sozopol which increased its bed resources by about 1000 beds. A five-star hotel Marina Palace was built whereby total village capacity reached 3 500 people. 2005 plans envisage a capacity of 4 500 people.

This season **Golden Sands AD** invested EUR 12 m in the resort. It is an owner of the resort's infrastructure – water supply and sewerage, electricity supply network, roads and alleys, as well as of 6 hotels. It also owns the Aqua polis water complex. The latest five-star hotel in Golden Sands – Admiral – was opened in early July. It was built only for five months, with investments exceeding EUR 10 m.

Golden Sands AD invests a portion of its assets in improving resort's infrastructure – expanding the sea-front alley, new modern pavement, decorating plants, new lighting. The dozens of stands along the sea-front alley will be removed; two new modern shopping centers will be built. Project completion is expected in 2005.

Legal Framework

Amendments to the Tourism Act were passed in the period under review. They envisage facilitated treatment **tour operators and tourist agents** by registration instead of licensing. The Minister of Economy assisted by a commission of experts will make tourist activity registrations. The state, the industry organizations of the nationally represented tourist associations will be equally represented in the commission.

The Minister of Economy will be responsible for the **categorization of tourist sites** as well and will be assisted again by a commission of experts involving industry organizations. Amendments include **beaches and ski-tracks** in tourist sites which makes them subject to compulsory categorization as well. Beaches will be categorized as A, B, and C, while ski-tracks as green, blue and red. These categories will be assigned based on with the minimum mandatory requirements for safety, information support, compliance with sanitary and hygiene standards and provision of tourist services. Categories will not be limited in time. The Council of Ministers will regulate in ordinances the organization, operation, maintenance, control and the categorization process. Categorization procedures for beaches and ski-tracks will be initiated on the basis of an application by the person who will provide tourist services for them. Procedures will be organized by a **special commission for categorization of tourist sites** to be set up **within the Tourism Agency.** It will comprise with equal votes representatives of the ministries of: economy; regional development and public works; agriculture and forestry; environment and waters; youth and sports, and the Tourism Agency on one part, and on the other part experts from the nationally represented associations and other non-profit legal persons engaged in the development of beaches and ski-tracks. A national association shall be any non-profit legal person uniting the companies doing tourist business in not less than 33 per cent of the categorized sites. Any category shall be terminated at the request of the owner or concessionaire in the event of its liquidation or bankruptcy and in the event of repeated violations.

The proposals to grant **national resort** status to some big Bulgarian resorts were not supported on second reading of the Amendments to the Tourism Act in the National Assembly. It was envisaged to have resorts divided in two categories, the one with a national resort status. The proposed definition characterized the national resort as "any settlement without permanent residents or independent territory, having separate infrastructure, which satisfies national tourism needs and meets the standards for such resort. Following lengthy debates this proposal and all other related proposals were dropped.

These proposals aimed at introducing clear rules and standards, higher order and responsibility for these resorts in terms of the construction and the quality of services and of the infrastructure. According to some experts, this was the way to put an end to indiscriminate construction, overloading with special infrastructure and disturbing the environmental balance. Unfortunately that has not been achieved for now.

It was announced that **an Act on the Black Sea Coast** regulating clear rules for the construction in and management of these resorts **will be passed by the end of 2004**.

Marketing and Advertising

The problems of national advertising and presenting Bulgaria abroad remained in the focus of discussions. **A forum on Bulgaria's national tourist advertising** was organized in Sofia at the end of April. Tourist organizations' representatives proposed to have one third of national budget revenues from tourism spend for advertising and the other portion – for improving the infrastructure. It was also proposed that Bulgaria should advertise its regions at international tourist exchanges, presenting the civil and regional tourism associations. According to experts, there is a need to make a comprehensive analysis of the Bulgarian tourist product, to define the target audience of messages, and to improve the knowledge of the specific needs and expectations of potential consumers. According to

MoE representatives, tourist advertising must be part of the overall strategy for presenting Bulgaria as a good place for living, business and entertainment. There is a need to target advertising not only towards foreign tourists and investors, but to Bulgarians as well.

The international tourist exchange ITB was organized in Berlin in March (12–16 March). Bulgaria participates for the 36 time. The Executive Agency for National Tourist Advertising and Information designed the national stand and was responsible for the overall organization. Twenty-eight Bulgarian companies and organizations from the tourism sector were presented within the stand. This forum is important for Bulgaria's preparation for the summer season and for attracting German tourists.

In the spring Bulgaria took part in **the international tourist exchange IETT organized in Moscow.** Forty-four Bulgarian companies from the tourism sector were presented on the national stand.

A conference on the problems of tourism and on the cooperation in the tourism sector was organized in Belgrade in May at deputy-ministers from the Balkan countries level. It was announced that the idea for a joint tourist product of the Balkans at the Summer Olympic Games in Athens will not be realized. This idea was formulated on previous conferences and political will for its realization was manifested. At this stage, however, its practical realization proved very difficult for a number of reasons, for example the existing visa barriers between the countries in the region.

Work is currently in progress on a bilateral basis – every country maintains bilateral relations with Greece and with the neighbor countries. There is a need to make this relationship multilateral. As a first step, each country will prepare specific proposals for events that can be organized simultaneously in the other countries of Southeast Europe as well. Bulgaria will formulate a proposal for **a joint tourist product** under the motto "The Balkan Road of Wine". Wine-making is a well developed sector in all countries in the region which can unite tourist companies. Joint tours of monasteries in the region can also be organized. At this stage Bulgaria and Greece offer such joint product.

In 2003 the nine countries of Southeast Europe signed a memorandum of understanding and cooperation in tourism. The objective is to facilitate the tourist flow in the countries of the region, to attract investments in this sector, to set up joint-ventures, to develop a joint tourist product and to exchange know-how for sustainable development of the tourism sector.

Condition of the Sector

Last year Agricultural Census results are not yet known, but **new agricultural producers registered** since the beginning of 2004 total some 53 thousand. While agricultural production gradually restores its positions, **the share of the sector** in the gross value added and the gross domestic product in Bulgaria has continued to decrease due to the accelerated development of the two other sectors – industry and services. According to latest data, in the first quarter of 2004 agriculture has accounted for about 6.5 per cent of GVA and 5.6 per cent of GDP. **Employment in the sector** registers decline and stands at about 8.2 per cent of total employment.

Latest data about the **condition of arable crops** indicate good yield for nearly all crops. The measures taken to provide agriculture with quality seeds, plant protection products, fertilizers and equipment will obviously produce the desired result. Total sown areas exceed 23 m decares, including some 9.6 m decares of wheat, over 1.9 m decares of corn, over 4.5 m decares of sunflower, and some 3.3 m decares of barley. The favorable agro-climatic conditions so far create prerequisites for relatively high yield in nearly all Bulgarian regions. Wheat yield is projected at over 3 m tons (against some 2 m in 2003), and sunflower yield - at over 800 thousand tons. Projected yield will guarantee higher export against last year and will improve the balance of trade.

The duty-free import of flour since the beginning of 2004 stabilized the market, put an end to the speculative price increase and had a favorable effect on the exchange trade in grain. It was clear as early as March that some 150 thousand tons of grain were available as a transitional balance till the new crop, which refuted the grain crisis thesis. While Government actions are aimed at maintaining the grain balance, Government intervention distorts the market and creates risks for the producers who cannot project the nature, time limit and scope of possible measures. The problem can be overcome by a more precise evaluation of the crop, more reliable statistics and further development of the grain warehouse notes as a necessary market infrastructure in the agriculture sector.

Environment for Development

On 4 June **Bulgaria closed the Agriculture Chapter of the negotiations with the European Union**. These negotiations continued for some 2 years and Bulgaria managed to agree quite favorable arrangements. The funds allocated to Bulgaria's agriculture in the financial framework, as well as the agreed quotas indicate the good assessment by the European Commission of Bulgaria's capacity to develop modern agriculture. The negotiation process was focused on the three basic priorities for Bulgaria: arable crops, vine-growing and wine-making, and animal breeding (particularly dairy cattle). Sector problems lie in the fact that negotiations register the situation as it is now, while producers rely on having this situation considerably changed in the future. Funds – EUR 1.55 b for the period 2007-2009, allocated for direct payments, market support (including intervention and export subsidies) and support for the rural regions – represent the maximum allocation from EU's budget. Actual drawing, however, is fully dependable on the sector's capacity to utilize these funds.

Work along three basic lines is needed with a view to ensure utilization of funds: setting up and strengthening a clear structure of agricultural producers and of their industry organizations; creating the necessary integrated control system (for example on farm land use, plants, number of animals), and setting up a payment agency to manage direct payments based on the integrated control system data. An intervention agency should be set up at the payment agency to balance the prices of the most sensitive goods for the purposes of consumer protection. Unlike the usual government intervention, the intervention agency should have clear operating rules and market intervention criteria, insofar as it its part of the Common Agricultural Policy mechanism.

The agricultural production subsidization system is gaining pace as a pilot mechanism for testing the European model. A subsidy for cultivating uncultivated private farm lands took effect since 1 March 2004. Total annual subsidy amounts to BGN 10 per decare. The State Fund Agriculture has also approved a financial framework for subsidizing some productions in 2004. Target subsidies are intended for produced and sold quantities of quality products. The amount of the export subsidies for producers selling on markets outside the EU has been determined. The 2004 subsidies for encouraging the export of processed agricultural products total BGN 3 m. Support will be provided preferentially to producers from the dairy sector. Companies should have export licenses with a view to receive export subsidies. The terms and procedure of issuing export licenses are regulated in Ordinance No. 2 to the Farmers Support Act[53]. The weak interest in export subsidies indicates that the model has not been polished and companies are not prepared to directly implement European models. In addition to the awkward procedure and the fixed export time limits, the guarantee amounting to 50 per cent of the subsidy, which is required for the issuance of export licenses, is another barrier to exporters. That called for reconsidering the conditions and lowering the guarantee to 20 per cent.

According to MAF's assessment, a decisive change in the interest towards **SAPARD** has been noticed since mid 2003. Intensified interest resulted in exhaustion of the amounts available for some measures. Four annual agreements have been signed to date, with agreed subsidy exceeding BGN 570 m. Over 1 200 projects have been approved so far, with total investment value exceeding BGN 1 b and agreed subsidy

53 Ordinance on the terms and procedure of paying export subsidies for the export of agricultural products, OG, No. 41/18 May 2004.

amounting to BGN 488 m. The amounts available for two SAPARD measures – processing enterprises and alternative activities, have been exhausted and funds have been reallocated from less implemented measures. Based on the measures laid down in the National Plan for Development of Rural Regions and the real interest in drawing the funds available from SAPARD, the SAPARD Agency and MAF requested additional subsidies. Thus the present annual amount of EUR 54 m will be completed with additional EUR 62.4 m for the next three years. 240 projects at a total value of BGN 290 m have been approved since the beginning of 2004 till mid June, with agreed subsidies amounting to BGN 123 m. Projects completed since the beginning of 2004 total 160, with paid subsidy amounting to BGN 45 m. Consideration of the new 750 projects deposited under the three SAPARD measures is pending. Given the limited program budget, not all of the projects will be classified for subsidies.

The problem with that aspect of the land reform, which concerns the **development of an agricultural cadastre and a register of estates,** remains outstanding. The lack of complete and precise information about the boundaries and location of estates, about their basic quantitative and qualitative characteristics, about the legal rights and limitations on such estates, prevent investments in agriculture and the development of agricultural production. The absence of a cadastre and the land fragmentation are a precondition for continuing higher supply on the land market. The USD 30 m loan provided from the World Bank accounts for 30 percent of the necessary funds for covering the whole territory of Bulgaria. The implementation of the cadastre and estate register project, which should be completed by March 2007, may well be delayed. The World Bank has insisted on urgent measures to speed up project implementation and fulfill undertaken commitments. The bank insists on a single agency of registrations and cadastre instead of the currently existing two independent bodies. Project implementation is expected to result in higher security for investments in agriculture.

At the end of April **the Parliament shelved the Forestry Company draft law introduced by MAF** and resolved on setting up a work group to develop a strategy for restructuring of the sector and a new draft law. The delay in **the Forestry sector reform** continues as a result of the conflict of interests in the management and control of wood production and trade. With a view to cut off the channels of illegal felling and unregulated export, the draft law provided for setting up a state forestry company responsible for state forests management and for the overall economic activity in forests. The draft law was shelved on account of market monopolization and centralized management which would disturb competition and abandon market mechanisms. The draft law was developed in cooperation with the World Bank, which assesses the set up of a state forestry company as complying with the good international practices in the industry. The bank is ready to allocate USD 30 m for project implementation, provided that the draft law gets passed and the reform gets started.

Several important events related to regional policy should be mentioned as we discuss the first half of this year – these are the European Commission's financial framework for Bulgaria; the closing of the Regional Policy Chapter of the country's EU accession negotiations; and the adoption on second reading of the Regional Development Act.

The European Commission adopted a decision – which was announced by the Commissioner responsible for Regional Policy and Institutional Reform - according to which **Bulgaria and Romania would receive 6 per cent of the total regional policy and structural funds over the 2007–2013 period** which means EUR 22 b. The planned financial framework for Bulgaria amounts to EUR 4.245 b for the transitional 2007–2009 period. The largest portion of this amount – EUR 2.3 b, will be spent on structural policies and improvement of the living standards. In experts' opinion this is one of the most favourable financial frameworks (vis-à-vis the territory and population) ever granted to a candidate country.

Bulgaria made a commitment to divide the country into **6 planning regions** and 28 regions. This was achieved through the new Regional Development Act which stipulates the mechanisms of regional planning. The allocation of financial resources from European funds will be made precisely on the basis of such planning, and also on the basis of the indicators for various populated areas and their most pressing problems. The six centers of administrative planning regions in the country are Burgas, Varna, Vidin, Ruse, Plovdiv and Sofia.

During the reviewed period several important pieces of legislation were adopted and promulgated: a new **Regional Development Act** (RDA); **Ordinance on the rules and regulatory standards for the development of the types of territories and spatial development areas**; **amendments to the Territorial Development Act.**

There are several reasons behind the special significance of the new Regional Development Act. The former Regional Development Act adopted in 1999 and the regulations to it were not in line with the provisions of EU Regulation 1260/1999 regarding the unified provisions on structural funds; the functions of bodies in charge of implementing the regional development policy were not adequately defined; some financial resource issues were not settled; the monitoring and evaluation system was not adequately regulated; no legal framework was in place to ensure the information servicing of regional development needs.

The new Act provides for the drawing up of a **National Regional Development Strategy** and the following **planning and program documents**: regional strategies and development schemes (NUTS 3 level); regional development plans (NUTS 2 level); municipal development plans (NUTS 4 level); National Operational Program for Regional Development (NOPRD). A new legal requirement is introduced establishing a connection between regional and territorial development planning at the national and regional level.

The establishment of **new planning and programming bodies** is also envisaged. These are the Regional Development Councils and the "Technical Cooperation, Coordination and Management of Regional Programs and Plans" Directorate at the NUTS 2 level and Regional Development Councils at the NUTS 3 level. A new wording is proposed for **target regions** – areas of economic growth, areas of industrial decline, underdeveloped border regions, underdeveloped rural regions, mountainous areas and areas of high unemployment.

The regulations to the new Regional Development Act are expected to be adopted shortly. The secondary legislation under the new RDA needs to further develop the latter's provisions and stipulate the requirements for the development, coordination, control and information aspect of planning documents and the activity of various authorities for its implementation.

The Act differentiates between strategic planning documents and documents providing for financing and implementation - this is one of the requirements of EU Regulation 1260/1999 laying down the general provisions on the Structural Funds. The combination of two basic planning approaches is characteristic of the new Act - the "top-down" approach and the "bottom-up" approach. The basic principle is that strategies for which no EU or state budget financing is secured will be developed "top-down" while plans will be drawn "bottom-up" for levels where funding/budget is secured.

At the national level there are plans to develop a National Economic Development Plan (NEDP) which will determine the macro framework and define strategic objectives and priorities of the economic development. The development of the NEDP was entrusted to the Agency for Economic Analysis and Forecasts under the MoF which presented in May its economic analysis and forecast for the country's macro-economic framework for the 2007–2013 period. The importance of NEDP in the process of EU Structural Funds absorption was emphasised.

For regional policy needs, there are plans to develop a National Regional Development Strategy which must be approved by the Council of Ministers upon proposal by the Minister of Regional Development and Public Works. This strategy will determine the framework of the National Operational Program for Regional Development. At the planning region level regional development plans will be developed and these will be the structural elements of the NOPRD.

At the regional level regional strategies and development and development schemes will be drafted which will be approved by the Regional Governor only upon prior coordination with the Regional Development Council and the Planning Region Development Council.

Municipal plans will be developed and individual projects (regional development and local projects) will be proposed at the municipal level. Municipal development plans will be drafted in compliance with the regional strategies and development schemes and will be adopted by municipal councils upon proposal by the Mayor of the respective municipality.[54]

The sources of financing for regional development are: the state budget, municipal budgets, natural persons and legal entities, international financial institutions. The planning regions and target regions may also be offered assistance in compliance with the State Aid Act and also through other channels of government support – grants to implement measures included in NOPRD, grants to cover part of the expenses for the acquisition of fixed assets, real estate and construction in progress which are private, state and municipal property, tax deductions as stipulated in the law, etc.

Currently regional development concepts are being drafted for the 6 planning regions – North-West, North Central, North-East, South-East, South Central and South-West. These six concepts are being drawn up by 6 inter-institutional workgroups and will be the basis of a comprehensive regional development concept for the country. They are expected to be finalised by end July. The regional development councils will operate in the centers of the six planning regions; these councils will identify the key priorities. A public procurement procedure **for preparing a project entitled "National Regional Development Strategy of the Republic of Bulgaria for the 2005-2015 period"** was initiated; the national concept of regional development will be used as the foundation of this strategy.

Public opinion polls show that **Bulgarian municipalities are not adequately familiar with the tools to obtain EU funding**. Most information on EU funds is available on the Internet but some municipalities have no access to it; there are conflicts between municipal and regional authorities; not uncommon are also instances when personal or partisan favouritism outweigh business considerations when developing projects; there is no capacity for the preparation of good projects; procedures are complicated and lack transparency; municipalities find it hard to provide project co-financing.

It was announced earlier this year that **for the first time 8 municipal projects were approved for financing under the SAPARD Program**. The projects are worth a total of approximately BGN 11 m, with half of that amount earmarked for repair works of municipal roads. The approved projects will be implemented in municipalities in underdeveloped rural areas with a potential to develop tourism. Tourism is one of the key sectors related to regional development which is supported by European funds. Efforts are focused on building the infrastructure and creating new tourist sites. The total value of existing projects in tourism exceeds EUR 30 m and within the multi-year planning under the PHARE Program for the 2004–2006 period about EUR 26 m are expected to be allocated for infrastructure building to locations with tourism development potential. The amounts to be allocated to regional projects in other areas also run at hundreds of millions of Euros. The issue now is how these funds will be managed - and to what extent Bulgaria has the capacity to do so. Very important in this aspect is the dialogue between the central government and local administrations. Ministries face problems in failing to provide sufficient information, there are obstacles also in local administrations which often lack adequate capacity to draw up good proposals and ensure the absorption of funds. Key obstacles to the preparation of projects include: difficulties in structuring the priorities; budgeting, planning and spending the funds; drawing up viable development plans.

Opportunities for the improvement of the social infrastructure, urban environment, renovation of public buildings and tourist sites provided by the **Beautiful Bulgaria Project** have been extended. It was announced in April that 278 projects will be implemented under Beautiful Bulgaria in 2004, worth BGN 24 m. 35 new municipalities will be involved in the project, thus bringing the total number of municipalities participating in Beautiful Bulgaria projects to 99. Among the most interesting sites to be renovated are the Bachkovo Monastery, the Balabanova House and the Palace in Balchik. Priority components under the 2004 project will be "Social Infrastructure" and "Regeneration of the Urban Environment". According to current plans, a total of 8 600 people will be employed in the projects.

In order to overcome problems associated with information servicing, the Ministry of Regional Development and Public Works has declared its readiness to conduct **training seminars on the SAPARD, ISPA, and PHARE Programs**. The Ministry of Agriculture and Forestry has launched a European Information Center at the MoAF premises to provide advice to producers and processing industry representatives on the measures under the SAPARD Program. The SAPARD Agency also opened a permanent consultancy office for municipalities applying for financing under public measures of European pre-accession programs.

It was also announced in March that **for the first time this year municipalities will be granted interest-free loans from the state budget in order to participate in the financing of projects for which EU funds are available**. The state will provide as an interest-free loan the entire amount for the project not in one go but in individual disbursements according to the project stages.

[54] More details on Bulgaria's regional policy and the philosophy behind the new Regional Development Act are availalbe in the article by Dr. Y. Stoyanov "Bulgarian Regional Policy in the Context of European Union Regional Policy", 2003

In connection with municipalities' applications for financing from various EU funds also of interest is **the proposal of NAMRB for the possible transfer of state property to municipalities**. It mostly applies to sites which were formerly managed by the Ministry of Defense or MoI – former barracks or former Border Police premises in border regions. The justification behind such a proposal is that the majority of such sites are currently neglected and are turning into ruins. Part of these could be transformed into social establishments and in this way municipalities will be able to apply for funding from the "Social Investment Fund" of the European Union, which supports the construction of social establishments. A preliminary list of such sites has been drafted with the municipalities requesting for these to be transferred into their ownership. At this stage about 3 000 sites are included in the list, but it has not yet been finalised. NAMRB proposes two options for the transfer of ownership – a) for the Council of Ministers, by a single act, to transfer the property in the drafted list of municipalities or b) for this to be done through amendments to the acts on state and municipal property. The rational use of municipal property would allow municipalities to become financially self-sufficient.

Another proposal in this line of thinking is for the state to provide municipalities with residential property where it does not belong to individual ministries. NAMRB members also say that proceeds could be channelled to municipal budgets. The public residential buildings are mostly managed at the local level in EU countries. Irrespective of the fact that its portion in Bulgaria is very small (as few as 3 per cent) it could be used more rationally.

Such transformation of ownership could be considered as a step to decentralisation and strengthening of local self-government.

Following a quiet period in the field of financial decentralisation, at the end of February MRDPW proposed a new approach to achieve this - a Concept on the institutionalisation of the dialogue between local and central authority and the establishment of a Council on Decentralisation. There are however conflicting opinions as whether such a Council is truly necessary in view of the fact that the established working group on financial decentralisation is working quite successfully and there is no need to create another institution. What needs to be done, however, is to define more clearly the weight of opinions and recommendations by this working group before the central authority.

The **process of upgrading administrative services provided to businesses and citizens in municipalities** is advancing. A year after two municipalities in the Burgas Region - Pomorie and Primorsko - took over the administration of local charges and taxes, three new municipalities in the same region will move on to administer their local taxes and charges. This is part of a project for reform in the tax administration which is expected to be completed in 2006. Municipal officials in the three towns will be in charge of administering the property taxes and waste-collection charges (sending notices on payable charges and fees, drawing up information statements, adjustments, issuance of real estate tax valuation certificates, issuance of certificates verifying that all taxes were duly paid). The tax administration will provide municipal authorities with the computer systems, software, databases and qualified staff; it will provide methodological support and expert assistance to local authorities.

The municipality of Shumen introduced a good practice example by launching an **information system to improve administrative services - entrepreneurs will be notified by SMS** when permits for various types of activities are issued. This service is provided free of charge and is the first of its kind in the country. The system facilitates business management and saves time and costs. The procedure will be applied for the issuance of licenses for trade in alcohol and cigarettes, certificates for the registration and categorisation of trading outlets and permits for non-standard working hours. This service is provided in the "Trade and Licensing" sector of the municipal office processing about 20 requests daily. The "Document Processing" module is currently being developed. It will cover the entire incoming and outgoing correspondence related to administrative services to businesses and citizens by the municipality of Shumen.

ENTERPRISE POLICY IN THE EUROPEAN UNION

Petar Stankov, Center for Economic Development

The negotiations for accession to the EU have been completed in the first half of 2004, which puts on the agenda a specific range of issues going beyond the process of aligning the Bulgarian legislation with the *acquis communautaire*. The issues, which the integration process brings forward, relate to various levels of the economy and of state governance. They also touch upon specific policies and practices which should be integrated in the Bulgarian economic policy with a view to create conditions to fully integrate the Bulgarian economy into the Common European Market.

The enterprise policy is a key economic policy in the EU, which the Center for Economic Development has aimed at studying in a couple of recent issues of the Bulgarian Economy Quarterly Report. The objective of this section is to present this policy on Community level and to draw wherever possible a parallel between what is topical in the EU, including the new Member States, and in Bulgaria with respect to this set of policies in different economic and state governance areas, called enterprise policy.

The administration of the European Commission regards the enterprise policy as **the basic tool for attaining the goals set at the Lisbon European Council in 2000** of making the EU, by 2010, the most competitive and dynamic knowledge-based economy in the world, capable of sustainable growth with more and better jobs and greater social cohesion.

The enterprise policy aims at encouraging EU and accession countries' economies to create a favorable business environment for the start up and operation of companies. Enterprise policy measures are focused particularly on SMEs, while big companies also benefit from the improved environment for doing business. However, direct incentives for enterprises are also used concurrently with this approach and totally in line with the regulativistic manner of European policy-making.

At supranational level in the EU the enterprise policy is organized on a horizontal basis, i.e. priority sectors are not outlined; there are only measures to improve the environment for start up, operation and withdrawal from business. At national level, however, these horizontal measures cannot fully guarantee the balance between the previous practices in the different economic policies of the Member States on one part, which are rather aimed at defining priority sectors and encouraging certain economic sectors, and the promotion of the business environment as a whole on the other part, which requires to think supranational in the adoption and application of sector policies within a Member State. It is natural that the corporate lobbies of the big "traditional" sectors in the EU are unwilling to give up their privileges on national level. That is why European Commission's analysts, who are also representatives of different Member States, arrive at the following compromise formulation of the enterprise policy methods: "Industrial policy instruments, which are those of enterprise policy, aim to provide the framework conditions in which entrepreneurs and business can take initiatives, exploit their ideas and build on their opportunities. However, it needs to take into account the specific needs and characteristics of individual sectors. It therefore needs to be applied differently, according to the sector. For example, many products, such as pharmaceuticals, chemicals, automobiles, are subject to detailed sector-specific regulations dependent on their inherent characteristics or use. Industrial policy therefore inevitably brings together a horizontal basis and sectoral applications."[55]

The horizontal aspect of the EU enterprise policy aims at improving the business environment in 8 dimensions, the influence on which is expected to result in achieving the Lisbon objectives:

- Access to financing;
- Regulatory and administrative environment;
- Open and effectively functioning markets;
- Entrepreneurial activity;
- Human resources;
- Innovation and knowledge diffusion;
- Information and communication technology; and
- Sustainable development.

Measures to improve the access to finance for SMEs in the EU[56]

The EU enterprise policy contains measures to improve the access to finance for SMEs. This support for SMEs is realized either directly by the EU or through the Union's Structural Funds, which are allocated to the different countries and are managed at national level.

The European Structural Funds are the main source of opportunities for SME financing, which the EU membership provides to the SMEs in a Member State. Their objective is to lessen the differences in the economic development of the regions of the EU in four basic areas: agriculture, regional policy,

55 Commission of the European Communities. Industrial Policy in an Enlarged Europe. Brussels, 11.12.2002 COM (2002) 714 final, p. 3

56 This part of the review is based on: European Commission. DG Enterprise. European Union Support Programs for SMEs. May 2003.

employment and social activities. Unlike direct subsidies, the funds are managed on national level. The projects with which SMEs apply for financing are nominated for financing by the Member State or by a region in the state. Four funds have been set up to support the accelerated development of less developed European regions: European Regional Development Fund, European Social Fund, European Guarantee Fund for Development of Agriculture, and Financial Instruments for Development of Fisheries.

Direct EU assistance for European enterprises is basically concentrated in three areas: environment, research and education. They are provided to SMEs by the different departments of the European Commission. SMEs can apply for financing under the direct financing programs, provided that they have submitted an international project generating certain value added. The assistance is in the form of subsidy covering 50 per cent of project costs. Examples of such programs include: the Sixth Framework Program for Research and Technological Development (2002 – 2006), where 15 per cent of program's budget will be allocated for support of research and innovations in SMEs, EURECA – a network for market-oriented research and development, and Socrates and Leonardo da Vinci in the area of education.

The third basic source of financing generated by the enterprise policy in the EU includes the various financial instruments, which are not directly accessible by enterprises. The funds are allocated by financial intermediaries from the corresponding Member State. These financial instruments have been created for the purpose of increasing the volume of loans to SMEs by: 1) encouraging banks to build up their own capacity for wider access of SMEs to their loans; 2) involvement in different loan schemes for the small and medium business, and 3) providing guarantees to institutions financing SMEs. EUR 320 million are envisaged for this area of the enterprise policy for the period 2001-2005. The funds are managed by the European Investment Fund.

Additional information on all basic aspects of the policy for improving the access to finance for SMEs in the EU is available in the local offices of the Euro Info Centers network.

Measures to improve the administrative and regulatory environment in the EU

The objective of the administrative and regulatory environment (ARE) improvement is to indirectly support the drive of potential entrepreneurs to take risks and to encourage the development of enterprises through institutional sources for positive change such as the performance of regulatory bodies, of the judicial system and of the various bodies implementing the enterprise policy. ARE is important for business development because the higher the number of barriers to the start up and development of business, the more difficult the enterprise growth, which is transferred as a macro effect onto GDP growth and aggregate demand, and as a secondary effect into slower enterprise growth.

In the EU the highest number of barriers exists in the regulations on recruiting new employees – this is the area of most considerable differences in the achievements of individual states. Different Member States have different number of recruitment procedures before and after starting work; the average EU level is 1 procedure before and 3 procedures after starting work.[57] The less the number of recruitment procedures, the highest the incentive for SMEs to grow.

Facilitated registration of companies registers considerable progress in recent years. In this area the basics parameters for positive change in the business environment are time and start-up costs, as well as subsequent time and costs of communicating with the administration. The shorter the time and the lower the costs of communicating with the administration, the higher the incentive for entrepreneurs to develop their business within the legal economy. In the EU the start up benchmark time and costs of a company are much lower (3 procedures and 1 day) compared to Bulgaria (10 procedures and 30 days)[58].

There are two other powerful methods to improve the administrative environment, which are widely used in the EU. The first is *the ex-ante and ex-post* analysis of the impact of legislation on business (the so-called *impact assessment analysis*). The leaders here are Ireland, Sweden and Great Britain, which have declared that by 2006 they will subject all business-related laws to such ex-ante and ex-post taking effect analysis. The second method is the *e-government*. Introducing ICT in public services is not an end goal in itself – it really lowers the costs of legal operation of the business thereby releasing resources for more investment and subsequent growth of jobs in the legal economy. In most countries the introduction of e-government is accompanied by campaigns to train entrepreneurs in using the new opportunities for business expansion and lower costs provided by ICT. In this respect the EU is also way ahead of Bulgaria as not less than 67 per cent of the public services are accessible via Internet (France); Denmark is the leader here because all public services in this country are usable via Internet[59].

Measures to improve the efficiency of markets

In the EU the measures to improve the functioning of markets are studied along three basic lines: (a) trade integration in and outside EU Member States; (b) state aid for specific enterprises;

57 OECD/EBRD. South East Europe Region: Enterprise Policy Performance. A regional Assessment. October 2003, p. 29.

58 EC. Benchmarking Enterprise Policy: Results from the 2003 Scoreboard. Brussels 4.11.2003, SEC (2003) 1278, p. 30.

59 Calculated as (Export+Import / 2 x GDP).

(c) transparent, open and highly advertised public procurement procedures.

EC studies reveal that new Member States present highest trade integration rates[60], with Estonia accounting for a share of about 80%, whereas Bulgaria – for about 40%[61]. These indicators are an evidence of both openness and competitiveness of their economies. Lower trade barriers (duties and non-tariff barriers) between EU Member States are basically used to improve trade integration.

The state aid for specific enterprises fades as a method of improving market efficiency, because the share of state aid in the economy registers a stable downward trend and varies between 0.5 per cent and 1.7 per cent of GDP in EU economies (calculated before the latest enlargement). Where measures in this area altogether exist, they shift from direct aid for specific enterprises to a horizontal approach, i.e. to providing framework conditions for efficient functioning of markets. The 2001 share of the "horizontal" state aid in total aid is about 70 per cent for the whole EU.[62] The national commissions for protection of competition and the implemented European legislation play a major role in this shift of approach.

Regarding the open and transparent public procurement procedures in the EU, Member States register the lowest progress in this area. The share of public procurement regarded as "open and transparent" for the whole EU is not more than 30 per cent; another feature of this process is the fact that a foreign rival of a local company participating in the tender can win rather as an exception (the share of public procurement won by a foreign company is only 1.3 per cent)[63]. This is indicative of an ongoing high asymmetry between the declared equality of economic agents in the EU and real practices, which are yet to make the big step to real integration of the European public procurement market.

Measures to encourage entrepreneurship

About 20.5 million enterprises operate in the EU (according to data before the latest enlargement again); 99.8 per cent of these are small and medium-sized, and 93.1 per cent of all enterprises have less than 10 employees and belong to the category of micro-enterprises[64]. The most important factors for encouraging entrepreneurship are the condition of the business environment and the personal qualities of entrepreneurs. One should not forget that there are two general types of entrepreneurs: 1) those who try to take advantage of a market opportunity they have noticed (opportunity entrepreneurs), and 2) those who become entrepreneurs for the need to support their families or for the personal belief that they must be architects of their own future (necessity entrepreneurs). Entrepreneurship as a perceived market opportunity is a result of the improved environment for start up and doing business and of the changed attitude of potential entrepreneurs towards risk. The transition towards this type of entrepreneurship is achieved by way of different types of training and developing further the human resources in the EU through permanent training in entrepreneurial skills.

Encouragement of entrepreneurship focuses on 6 major areas:

- Facilitating the start-up of enterprises;
- Improving the propensity towards entrepreneurship;
- Lowering the time and costs for business start up;
- Encouraging female entrepreneurship;
- Encouraging business incubators;
- Facilitating the transfer of ownership of SMEs.

It is clear that at least three of these areas are interrelated: the start up of enterprises, the time and costs, and the business incubators. The start up of enterprises is facilitated by lowering the time and cost of registration of companies; here the standard enterprise policy measure is the one-stop shop in which a company registration takes 1 day with only 3 standard procedures. As noted above, at the end of 2003 the values of these indicators for Bulgaria are 30 days and 10 procedures accordingly.

Overall, candidate countries achieve better results against Member States in the start- up of new companies and in keeping them on the market. The standard indicator employed to analyze start-up enterprises is *the net birth rate* (start-ups minus bankrupts[65]). For the period 1995-2000 this share is between –1.7 per cent and 6 per cent for the EU, whereas for candidate countries it is between 2.3 and 21 per cent[66]. This highlights the relation between the pace at which an economy is restructured and the emerging new opportunities for business which potential entrepreneurs in candidate countries make use of.

Regarding the promotion of female entrepreneurship, assessments in the EU are that this part of the population has not realized in full its potential for participation on the labor market. Total enterprises established by women in the EU account for not more than 28 per cent, for new Member States this share is 30 per cent, and in Bulgaria women are generally doing much better: the 2001 share of enterprises established by women is about 33-34 per cent[67].

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60 Calculated as (Export+Import / 2 x GDP).

61 Ibid, p. 34

62 Ibid, p. 36. An important methodological specification should be made here: in calculating state aid the aid for agriculture, fisheries and transport, which is sizeable in itself, is not included.

63 Ibid, p.36

64 Schmiemann, M. Enterprises in Europe – does size matter? // Industry, Trade and Services. Statistics in Focus, theme 4-39/2002, p.2

65 As share in total enterprises.

66 EC. Benchmarking Enterprise Policy: Results from the 2003 Scoreboard. Brussels 4.11.2003, SEC (2003) 1278, p. 41

67 Ibid, p. 45.

The propensity towards entrepreneurship is influenced by several factors: the public image of entrepreneurship, the traditions in entrepreneurship, the propensity towards risk, the market-generated opportunities, and the alternative income from employing the potential entrepreneur. In the EU the positive image is encouraged by positive media campaigns, by including entrepreneurship school subjects in secondary school and university curricula, and by horizontal measures to facilitate sector entry. Nevertheless, a conclusion can be made that the propensity towards entrepreneurship in the EU is lower than in the USA. In the USA risk is better received and the propensity to use entrepreneurship again as an opportunity for personal fulfillment even after failure is higher, while the fear of failure is lower than in the EU.

It is this risk aversion that makes the specific measure called "business incubators" so attractive for European policy-makers. While it does not belong to the group of horizontal measures for supporting entrepreneurship because it targets basically start-up high-tech companies and companies with high growth potential, these measures resulted in about 900 business incubators in the EU most of which operate through the support of government institutions and do not generate profit[68]. The occupancy rates of business incubator areas in the EU vary between 44 and 100 per cent, which indicates a positive attitude to this measure by entrepreneurs and shows that it can be employed in the accession countries with a view to further encouraging entrepreneurship in high value added sectors.

Human resource policies

EC highlights a couple of measures to encourage the adequate response of the European education system to the demands of a knowledge-based economy. The first measure is the mutual recognition of secondary and university education diplomas in the Member States, which encourages labor force mobility. On the other hand, geographical mobility is not the only aspect of the mobility demanded by a knowledge-based economy. Re-qualification and change of profession is normal practice and therefore programs for permanent training in entrepreneurship and high technology are encouraged.

Surveys reveal that new Member States and candidate countries are ahead of old EU Member States only in terms of the number of graduates in social sciences, and in isolated cases like Lithuania, Romania and Slovenia – in terms of the number of graduates in technical sciences. In the other areas of human resource development, which support the knowledge-based economy, like mathematics, computer sciences and medicine, new Member States trail far behind the average EU values. Bulgaria is way ahead the average EU values only in terms of the number of graduates in social sciences, but in the other new economy-related areas of education the country is also lagging far behind[69].

Policies for innovation and knowledge diffusion

To attain its objective of becoming the most competitive and dynamic knowledge-based economy in the world, Europe should find the proper policies for guaranteed wide innovation and knowledge diffusion, because these provide the short-cut to company competitiveness, which in turn builds up the competitiveness of the Member States, hence of the EU and its economy. Europe is lagging behind the USA and Japan in terms of the share of R&D in GDP, particularly in terms of the business-generated share of R&D in GDP. Only the economies of Finland and Sweden are ahead of the USA in terms of business R & D. European economies allocate between 0.7 and 3.8 per cent of GDP for R & D, thus making the average EU level only 1.9 per cent[70]. To encourage the facilitated transfer of research developments to the business, which would allow having the strategic objective of 3 per cent R & D in GDP attained by 2010, European policy-makers are ready to see expanded government functions in this area. This is also proven by the fact that between 4 and 14 per cent of companies' R & D costs are financed by the governments of the Member States. Yet one should not forget also the opportunities mentioned in the beginning – participation of European SMEs in different knowledge diffusion promoting programs at supra-national level.

Two trends of government participation in the financing of innovation and knowledge diffusion, in R&D costs accordingly, are observed in the new Member States and the candidate countries. The first trend is formed by countries like Cyprus, Hungary, Latvia and Slovenia whose governments do not seem interested in high involvement in the financing of business R & D programs: in these countries direct government transfers for R & D are not more than 6-7 per cent. Despite that, Slovenia is ranked top among candidate countries together with Estonia in terms of: R&D costs in GDP, Internet-users and subscribers to mobile operators[71]. This fact plus the fact that Estonia belongs to the second group of states whose governments are more inclined to finance technology transfer business undertakings indicates that a universal policy satisfying local business requirements and thereby allowing local companies to allocate more funds for R&D is hardly possible to formulate. Yet Estonia is an unquestionable leader among candidate countries in terms of the changes in the regulatory framework for innovation: it was the first to pass the electronic signature act and to liberalize its telecommunications market, and these prove important indirect factors for innovation and knowledge diffusion. The above mentioned second group of countries

68 Source: European Commission. Benchmarking Enterprise policy. Results from the 2002 scoreboard. Commission staff working document. SEC (2002) 1213, Nov. 2002, p. 50.

69 European Commission. Benchmarking Enterprise policy. Results from the 2002 scoreboard. Commission staff working document. SEC (2002) 1213, Nov. 2002, p. 62

70 Calculated again on EU 15.

71 Kalvet, Tarmo. Estonians and Slovenians at Top in IT. The Baltic Review. Vol.19. http://www.tbr.ee/issues/vol19/it_top.html

with more active state involvement includes Estonia as well as Bulgaria, the Czech Republic, Slovakia, Poland and Romania. In this group the share of state participation is between 14 and 38 per cent, with Romania being at the top[72].

Encouraging the production of new patents and their transfer into real business practices, as well as the policies for promoting the export of high-tech products are also elements of the enterprise policy in the old and new EU Member States (including candidate countries). The difference between the two groups is that the new Member States are lagging far behind old Member States in terms of the number of patents per 1 m people (with the exception of Slovenia) and in terms of the share of high-tech export.

Pursuing certain quantitative targets is not an exception in the policies of EU Member States. Besides, these definitely yield positive results provided that they are linked to policies which are adequate to the specific national conditions and include the growth of the scientific potential in technical sciences, intellectual property protection, applying cluster strategies for development of certain sectors and regions, and encouraging venture capital. Finland, for example, has been applying such quantitative targets since the 1970-ies, reaching in the beginning of this century the level of the most competitive economy in the world[73].

Policies for ICT diffusion

These policies are closely related to those discussed in the previous paragraph, for employing specific measures for innovation and knowledge diffusion implies encouraging ICT as well. Some more specific measures are taken in the EU: encouraging ICT penetration in every economic sector, improving the importance of e-commerce, improving the Internet access, particularly broadband access, of enterprises and encouraging the competitiveness of Internet providers with a view to decrease the Internet access costs of companies.

Sustainable development as a policy element

While sustainable development is defined as the simultaneous impact of economic, social and environmental factors on the condition of European enterprises, talks in the EU are focused mainly on the third component. This is so because firstly, the economic measures discussed above are quite comprehensive; secondly, there are vast differences between the social systems within the EU, and thirdly, the normative implementation of environmental production standards is rather simple for the whole EU. It is on this area that the EU enterprise policy is focused: environmental pollution and environmental management standards are adopted for EU enterprises in general (EMMA and ISO 14001). Measures to lower the energy intensity of productions and to reduce the emissions of noxious gases in the air are also implemented. Overall, candidate countries trail behind EU Member States in terms of the sustainable development indicators, with Slovenia being the only exception.

Completed negotiations for Bulgaria's accession to the EU normatively level up the formulation and implementation of economic policy instruments in Bulgaria. The indicative goal of making the EU, by 2010, the most competitive and dynamic knowledge-based economy in the world requires Bulgarian policy-makers to synchronize good practices on Common Market level in developing the measures of Bulgaria's enterprise policy. This means work on all aspects of the enterprise policy with systematic measures.

In the past year Bulgaria witnessed significant positive changes towards encouraging entrepreneurship and investment, facilitating the access to finance, opening an increasing number of markets outside EU for Bulgarian goods and improving the trade integration with the EU. Yet this positive development of the enterprise policy cannot compensate the lag behind most new Member States and the EU-15 in terms of a number of regulatory environment parameters, ICT diffusion in business and households, innovation and knowledge diffusion, reforming the education system towards building entrepreneurial skills. These weaknesses of Bulgaria's enterprise policy should be overcome in the process of integrating Bulgaria's economy with EU economy and their transition towards the most competitive economy in the world.

72 European Commission. Benchmarking Enterprise policy. Results from the 2002 scoreboard. Commission staff working document. SEC (2002) 1213, Nov. 2002, p. 67

73 Ref. Global Competitiveness Report 2003-2004, p.2

Economic dynamics

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Industry													
Industrial production, volume index, previous month =100, %													
2004	85.4	105.8	113.2	89.2									
2003	86.5	96.7	116.7	91.8	94.6	111.8	103.1	93.7	109	102.2	99.5	112.6	-
Industrial production, volume index, corresponding month of the previous year = 100, %													
2004	112.7	120.6	117.8	113.6									
2003	115.4	115.4	123.4	111.9	109.6	115.4	113	110.3	115.9	117.9	111.3	123.5	-
Industrial production, from the beginning of the year, volume index, corresponding period of the previous year = 100, %													
2004	116.1	118.4	117.8	116.8									
2003	115.4	115.4	118.2	116.4	115	115.4	115	114.4	114.5	114.8	114.5	115.2	-
Industrial sales, total, volume index, previous month =100, %													
2004	84.2	110.1	114.7	94.2									
2003	86.2	96.8	119.6	92.6	98.5	108.8	102.5	93.9	106.3	103.4	98.2	111	-
Industrial sales, total, corresponding month of the previous year = 100, %													
2004	111.4	124.1	119.1	121.1									
2003	117.7	116.4	130.4	111.3	117.8	118.3	113.4	111.4	116.3	121.5	114.4	121.3	-
Industrial sales, total, from the beginning of the year, volume index, corresponding period of the previous year = 100, %													
2004	111.4	117.6	118.1	118.9									
2003	117.8	117.1	121.6	118.8	118.6	118.6	117.7	116.9	116.8	117.3	117	117.4	-
Domestic trade													
Trade and repairing activities, total, net receipts from sales, volume index, previous month =100, %													
2004	82.2	106.1	102.4	99.4									
2003	71.0	102.7	107.1	101.7	102.6	102.9	106.5	98.2	104.2	102.7	96.8	114.4	-
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, previous month =100, %													
2004	79.7	107.4	107.6	105.6									
2003	76.7	98.0	107.3	102.7	103.4	107.0	105.9	100.1	102.8	105.2	99.2	108.1	-
Wholesale and commission trade, net receipts from sales, volume index, previous month =100, %													
2004	83.9	106.7	100.7	97.9									
2003	70.2	104.1	106.7	101.2	102.2	102.2	107.1	97.3	104.8	102.3	96.4	114.7	-
Retail trade, repair of personal and household goods, net receipts from sales, volume index, previous month =100, %													
2004	75.1	101.5	109.5	103.0									
2003	71.0	98.9	109.4	104.1	104.3	103.4	103.7	101.1	102.5	103.0	96.9	117.4	-
Trade and repairing activities, total, net receipts from sales, volume index, corresponding month of the previous year = 100, %													
2004	114.1	114.4	112.8	112.5									
2003	106.1	107.2	108.1	110.0	110.1	108.0	107.2	104.6	105.7	104.9	102.4	105.8	-

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, corresponding month of the previous year = 100, %													
2004	111.9	111.3	112.3	121.9									
2003	103.5	98.8	100.6	101.2	102.5	104.1	103.8	102.3	103.1	103.9	101.5	105.2	-
Wholesale and commission trade, net receipts from sales, volume index, corresponding month of the previous year = 100, %													
2004	114.5	114.9	113.0	111.4									
2003	107.5	109.5	109.8	112.0	112.2	109.0	107.7	104.6	105.8	104.5	101.7	105.5	-
Retail trade, repair of personal and household goods, net receipts from sales, volume index, corresponding month of the previous year = 100, %													
2004	113.1	113.9	111.5	112.1									
2003	102.0	102.1	104.4	106.4	105.5	105.9	106.9	106.2	106.9	108.1	106.3	108.0	-
Trade and repairing activities, total, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %													
2004	114.1	114.2	113.6	113.3									
2003	106.1	107.8	108.0	108.7	109.0	108.8	108.5	108.0	107.7	107.4	106.9	106.7	-
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %													
2004	111.9	111.4	111.7	114.3									
2003	103.5	101.5	101.2	101.3	101.6	102.1	102.3	102.3	102.4	102.6	102.5	102.8	-
Wholesale and commission trade, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %													
2004	114.5	114.7	114.0	113.3									
2003	107.5	109.7	110.0	110.7	111.0	110.7	110.2	109.4	108.9	108.4	107.7	107.5	-
Retail trade, repair of personal and household goods, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %													
2004	113.1	113.5	112.6	112.4									
2003	102.0	102.6	103.3	104.0	104.3	104.6	105.0	105.2	105.4	105.7	105.7	106.0	-
Inflation													
Inflation (Consumer price index - 100), previous month =100, %													
2004	1.4	0.3	-0.1	0.3	0.0								
2003	0.6	0.1	0.4	0.3	-0.6	-2.2	0.9	0.8	0.9	0.7	1.8	1.8	-
Inflation (Consumer price index - 100), December of the previous year = 100, %													
2004	1.4	1.7	1.7	1.9	2								
2003	0.6	0.8	1.2	1.5	0.8	-1.4	-0.5	0.3	1.2	1.9	3.8	5.6	-
Inflation (Consumer price index - 100), corresponding period of the previous year = 100, %													
2004	6.4	6.6	6.2	6.1	6.8								6.4
2003	1.7	0.2	-0.2	0.3	1.7	1.3	2.0	3.5	3.6	3.3	5.1	5.6	0.6
Employment and unemployment													
Unemployed persons registered, total, end of the period, number													
2004	537 137	527 258	507 508	487 814	466 717								507 508
2003	646 757	611 727	581 350	552 068	528 718	506 424	489 343	480 881	472 614	476 326	489 618	500 664	581 350

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Unemployment (Employment Agency, ratio to the economically active population from the population census in 2001), end of the period, %													
2004	14.50	14.23	13.70	13.17	12.60								13.7
2003	17.46	16.51	15.69	14.9	14.27	13.67	13.21	12.98	12.76	12.86	13.22	13.52	15.69
Newly opened vacant jobs, for the period, number													
2004	3 286	4 772	5 050	3 538	4 090								5 050
2003	1 759	2 024	2 136	2 480	2 349	6 076	3 890	2 782	2 804	3 365	3 516	3 999	2 136
Employed persons, total, end of the period, number													
2004	2 077 939	2 097 911	2 118 484										2 118 484
2003	1 946 834	1 991 623	2 016 828	2 043 764	2 054 972	2 068 694	2 075 881	2 067 291	2 063 429	2 050 282	2 034 033	2 005 369	2 016 828
Employed persons, public sector, end of the period, number													
2004	751 581	759 430	766 602										766 602
2003	730 873	757 271	765 688	771 192	771 746	775 281	778 647	776 774	778 293	772 629	768 505	758 795	765 688
Employed persons, private sector, end of the period, number													
2004	1 326 358	1 338 481	1 351 882										1 351 882
2003	1 215 961	1 234 352	1 251 140	1 272 572	1 283 226	1 293 413	1 297 234	1 290 517	1 285 136	1 277 653	1 265 528	1 246 574	1 251 140
Fiscal review													
State budget													
Revenues of the Consolidated State Budget, total, BGN million													
2004	1 126.0	2 110.6	3 636.8	5 097.6									3 636.8
2003	1 029.2	1 944.8	3 220.6	4 631.2	5 813.3	6 830.5	8 054.1	9 158.9	10 311.4	11 573.2	12 657.0	14 072.0	3 220.6
Expenditures of the Consolidated State Budget, total, BGN million													
2004	1 152.7	2 260.2	3 408.4	4 568.7									3 408.4
2003	1 130.6	2 105.4	3 109.8	4 221.5	5 195.0	6 203.4	7 402.7	8 429.7	9 463.7	10 602.5	11 758.1	14 071.1	3 109.8
Consolidated State Budget deficit (-) /surplus (+), BGN million													
2004	-26.7	-149.5	228.4	528.9									228.4
2003	-101.5	-160.6	110.8	409.7	618.3	627.1	651.4	729.2	847.8	970.7	898.9	0.9	110.8
Revenues of the Republican Budget, total, BGN million													
2004	777.1	1368.7	2343.4	3368.2									2 343.4
2003	651.3	908.4	1937.0	2878.1	3626.4	4221.2	4985.2	5637.7	6279.0	7051.8	7684.9	8441.6	1 937.0
Expenditures of the Republican Budget, total, BGN million													
2004	841.2	1531.5	2222.5	2963.0									2 222.5
2003	737.0	1195.6	1846.2	2594.1	3016.6	3639.2	4372.7	4979.0	5520.4	6200.7	6952.7	8552.2	1 846.2
Republican Budget cash deficit (-) / surplus (+), BGN million													
2004	-64.0	-162.8	120.9	405.3									120.9
2003	-85.7	-287.2	90.8	284.0	609.7	582.0	612.4	658.7	758.5	851.1	732.2	110.6	90.8
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1

(Continued)

Government and government guaranteed debt													
Government and government guaranteed debt, BGN million													
2004	16 731.7	16 852.8	17 032.7										17 033
2003	17 547.9	17 638.7	17 560.2	17 679.7	17 062.1	17 364.8	17 466.7	17 858.3	17 194.7	17 140.1	16 930.8	16 509.7	17 560
Domestic government and government guaranteed debt, BGN million													
2004	2 331.3	2 397.3	2 425.6										2 426
2003	2 113.5	2 207.4	2 290.7	2 246.2	2 225.5	2 233.9	2 215.4	2 236.5	2 218.1	2 193.7	2 248.4	2 241.2	2 291
Foreign government and government guaranteed debt, BGN million													
2004	14 400.4	14 455.5	14 607.1										14 607
2003	15 434.4	15 431.3	15 269.8	15 433.7	14 836.3	15 131.1	15 251.2	15 621.8	14 976.6	14 946.6	14 683.4	14 268.6	15 270
Government and government guaranteed debt, ratio to the annual GDP, %													
2004	44.1	44.4	44.8										44.8
2003	49.7	50.0	49.8	50.1	48.4	49.2	49.5	50.6	48.7	48.6	48.0	47.8	49.8
Domestic government and government guaranteed debt, ratio to the annual GDP, %													
2004	6.1	6.3	6.4										6.4
2003	6.0	6.3	6.5	6.4	6.3	6.3	6.3	6.3	6.3	6.2	6.4	6.5	6.5
Foreign government and government guaranteed debt, ratio to the annual GDP, %													
2004	37.9	38.1	38.5										38.5
2003	43.7	43.7	43.3	43.7	42.0	42.9	43.2	44.3	42.4	42.4	41.6	41.3	43.3
Domestic government debt, total, BGN million													
2004	2 331.3	2 397.2	2 425.7										2 426
2003	2 111.6	2 205.8	2 289.4	2 245.3	2 225.1	2 233.9	2 215.5	2 236.5	2 218.2	2 193.6	2 248.4	2 241.1	2 289
Debt on Government Securities issued for budget deficit financing, BGN million													
2004	1 822.7	1 889.3	1 914.9										1 915
2003	1 515.4	1 608.5	1 696.0	1 658.9	1 658.5	1 658.2	1 637.7	1 652.5	1 653.9	1 633.2	1 696.7	1 703.9	1 696
Debt on Government Securities issued for structural reform, BGN million													
2004	508.6	508.0	510.8										511
2003	596.2	597.2	593.4	586.4	566.6	575.7	577.7	584.0	564.3	560.4	551.6	537.2	593
Domestic government guarantees, BGN million													
2004	0	0	0										0
2003	1.8	1.5	1.2	0.9	0.5	0	0	0	0	0	0	0	1.2
Foreign government debt, USD million													
2004	8 620.0	8 635.2	8 587.7										8588
2003	8 109.3	8 091.6	8 090.0	8 355.8	8 535.8	8 414.6	8 372.2	8 284.1	8 461.0	8 417.2	8 530.4	8 718.6	8090
Foreign government guaranteed debt, USD million													
2004	498.1	542.9	541.8										542
2003	426.3	415.3	416.0	427.8	432.0	425.8	453.4	443.6	461.3	464.3	473.5	495.5	416

(Continued)

Foreign economic relations and foreign investments

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Balance of Payments													
Current account, million USD													
2004	-291.8	-157.3	-167.8										-616.9
2003	-164.9	-156.0	-93.6	-388.3	-222.7	33.3	33.1	146.1	17.1	-225.9	-316.0	-328.4	-414.5
Trade balance, (FOB), million USD													
2004	-191.8	-183.3	-267.4	-326.4									-642.5
2003	-71.3	-121.3	-117.6	-267.0	-287.3	-159.2	-207.8	-159.1	-148.6	-249.6	-322.0	-363.0	-310.2
Exports (FOB), million USD													
2004	620.6	733.9	813.4	729.0									2167.9
2003	544.2	538.7	642.9	570.6	568.0	657.0	717.6	618.1	651.7	677.0	634.3	618.4	1725.8
Imports (FOB), million USD													
2004	812.4	917.2	1080.8	1055.4									2810.4
2003	615.5	660.0	760.5	837.6	855.3	816.2	925.4	777.2	800.3	926.6	956.3	981.0	2036.0
Services, net, million USD													
2004	-26.3	-3.5	-21.2										-51.0
2003	-21.7	-14.4	-24.5	-35	33	169.3	237.4	237.7	124.8	-21	-45.5	-39.7	-60.6
Income, net, million USD													
2004	-132.3	-23	6.1										-149.2
2003	-113	-48.1	-19.6	-132.9	-13.4	-27	-61.4	-4.8	-39.2	-4.5	-2.3	-18.5	-180.7
Current transfers, net, million USD													
2004	58.6	52.5	114.7										225.8
2003	41.1	27.8	67.9	46.6	45.1	50.3	64.8	72.3	80.1	49.3	53.7	92.8	136.8
Capital account, million USD													
2004	0	0	0										0.0
2003	0	0	0	0	0	0	0	-0.1	-0.1	-0.1	0	0	0.0
Financial account, million USD													
2004	-98.3	379.3	258.6										539.6
2003	-9	81.4	120	502.2	221.7	122.1	-51.1	50.3	80.9	473.6	163.8	97.1	192.4
Direct investment abroad, million USD													
2004	-6	-1.4	-9.5										-16.9
2003	-0.5	-0.4	-1.6	-2.6	0.7	-2.2	-1.9	-4.8	-2	-2.9	-0.5	-3	-2.5
Direct investment in Bulgaria, million USD													
2004	126.4	82.6	157.7										366.7
2003	86.5	65.5	127.2	149.8	190.3	104.5	163.9	74.6	74.5	326.4	-1.5	57.7	279.2

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Portfolio investment assets, million USD													
2004	-64.3	-17.2	36.5										-45.0
2003	13	10	-19.9	10.5	86.5	-36.6	-87.2	-55.3	28.2	-36.7	24.7	-10.1	3.1
Portfolio investment liabilities, million USD													
2004	-85.9	-44.7	46.5										-84.1
2003	-32	-3.3	-29.8	0.4	30.2	-1.4	-87.9	-16.1	10.2	-14.8	5.6	4.4	-65.1
Other investment assets, million USD													
2004	-125.1	141	-60.6										-44.7
2003	-15.1	34.7	-60	256.7	-140	-36.4	-47.2	96.4	-145.6	163.5	88.9	-48.3	-40.4
Other investment liabilities, million USD													
2004	56.5	219	88.1										363.6
2003	-60.8	-25	104.2	87.4	54.1	94.3	9.1	-44.5	115.6	38.1	46.7	96.4	18.4
Net Errors and Omissions (BP), million USD													
2004	12.7	-79.2	112.2										45.7
2003	-125.9	119.7	56	61.1	105.9	-87.5	16.4	-76.7	-23.2	83.4	260.7	156	49.8
Overall balance (BP), million USD													
2004	-377.4	142.8	202.9										-31.7
2003	-299.8	45.1	82.3	175.1	104.9	67.8	-1.6	119.5	74.7	331.1	108.4	-75.4	-172.4
Reserves and Related Items, million USD													
2004	377.4	-142.8	-202.9										31.7
2003	299.8	-45.1	-82.3	-175.1	-104.9	-67.8	1.6	-119.5	-74.7	-331.1	-108.4	75.4	172.4
Finance													
Financial indicators													
Exchange rate BGN / USD, average for the period													
2004	1.549	1.546	1.594	1.633	1.631								1.564
2003	1.842	1.815	1.810	1.803	1.683	1.677	1.720	1.756	1.745	1.672	1.671	1.593	1.823
Exchange rate BGN / USD, end of the period													
2004	1.579	1.575	1.599	1.637	1.603								1.600
2003	1.808	1.813	1.795	1.757	1.654	1.711	1.728	1.789	1.678	1.682	1.630	1.548	1.795
Basic interest rate, effective annual, average for the period													
2004	2.79	2.49	2.41	2.55									2.56
2003	3.23	2.50	2.53	2.57	2.95	2.89	2.52	2.53	2.57	2.59	2.60	2.67	2.75
Money (M1), BGN million													
2004	7 788.4	7 852.5	7 835.1	7 987.2									7 835.1
2003	6 291.4	6 376.6	6 274.3	6 434.6	6 559.6	6 834.4	7 110.4	7 314.3	7 416.4	7 421.7	7 376.6	8 029.9	6 274.3

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Money (M2), BGN million													
2004	16 439.0	16 655.3	16 678.5	17 081.5									16 678.5
2003	13 550.9	13 722.5	13 541.5	13 762.2	13 765.6	14 197.2	14 623.8	15 045.6	15 073.2	15 698.1	15 604.7	16 464.7	13 541.5
International reserves of BNB, BGN million													
2004	9 841.4	10 112.3	10 494.3	10 605.1									10 494.3
2003	8 363.2	8 472.8	8 602.7	9 233.3	9 315.7	9 451.3	9 517.7	9 799.7	9 881.9	10 413.4	10 556.8	10 382.8	8 602.7
Fiscal reserves at the Issue Department of BNB, BGN million													
2004	3 138.4	3 146.7	3 503.2	3 822.5									3 503.2
2003	2 793.2	2 803.8	3 027.5	3 632.7	3 873.1	3 747.4	3 766.3	3 767.3	3 831.5	3 970.8	4 176.6	3 280.1	3 027.5
Banking system													
Claims on credits granted by the Commercial Banks, total, BGN thousand													
2004	9565122 [1)]	9 848 840	10 247 405	10 659 517									10 247 405
2003	6 444 818	6 563 130	6 816 766	7 167 024	7 424 452	7 727 590	7 866 307	8 171 994	8 471 157	8 904 325	9 114 301	9 454 164	6 816 766
Credits to Resident Sector, total													
2004	9 465 473	9 747 743	10 131 312	10 545 411									10 131 312
2003	6 356 088	6 489 721	6 745 467	7 094 504	7 355 881	7 657 439	7 797 284	8 092 008	8 391 057	8 832 873	9 044 229	9 352 878	6 745 467
Credits to Government Sector													
2004	24 891	27 795	26 973	26 451									26 973
2003	8 673	8 947	9 494	9 380	9 406	9 561	11 924	13 394	19 928	21 667	22 168	24 635	9 494
Credits to Non-government Sector													
2004	9 440 582	9 719 596	10 104 001	10 518 659									10 104 001
2003	6 291 902	6 444 260	6 662 763	7 014 528	7 280 799	7 603 463	7 727 111	8 030 421	8 325 688	8 751 119	8 977 126	9 303 120	6 662 763
Credits to Non-financial Public Corporations													
2004	-	245 972	231 880	232 625									231 880
2003	219 215	229 954	235 631	246 234	245 746	231 489	245 251	237 021	230 292	213 420	217 489	234 230	235 631
Credits to Non-financial Private Corporations													
2004	6785654 [2)]	6 685 783	6 932 080	7 194 675									6 932 080
2003	4 715 900	4 800 569	4 949 708	5 202 209	5 377 904	5 604 204	5 575 897	5 774 664	5 956 901	6 287 344	6 412 770	6 641 717	4 949 708
Credits to Households and NPISH													
2004	2 530 436	2 655 236	2 802 335	2 950 438									2 802 335
2003	1 260 492	1 300 531	1 355 108	1 438 127	1 532 501	1 645 779	1 758 072	1 853 587	1 933 809	2 035 462	2 116 719	2 201 298	1 355 108
Credits to Non-bank Financial Institutions													
2004	124 492	132 605	137 706	140 921									137 706
2003	96 295	113 206	122 316	127 958	124 648	121 991	147 891	165 149	204 686	214 893	230 148	225 875	122 316

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Credits to Monetary Financial Institutions													
2004	-	352	338	301									338
2003	55 513	36 514	73 210	70 596	65 676	44 415	58 249	48 193	45 441	60 087	44 935	25 123	73 210
Credits to Non-resident Sector													
2004	99 649	101 097	116 093	114 106									116 093
2003	88 730	73 409	71 299	72 520	68 571	70 151	69 023	79 986	80 100	71 452	70 072	101 286	71 299
Total assets, end of the period, BGN thousand													
2004	17 530 661	18 005 393	18 756 066	19 144 405									18 756 066
2003	14 470 798	14 527 980	14 976 602	14 754 441	14 752 332	15 359 751	15 706 435	16 019 647	16 386 230	16 621 238	16 608 301	17 323 643	14 976 602
Total liabilities , end of the period, BGN thousand													
2004	15 198 323	15 634 800	16 340 560	16 727 099									16 340 560
2003	12 413 277	12 474 347	12 882 639	12 702 089	12 694 628	13 252 494	13 584 220	13 870 342	14 218 293	14 410 754	14 364 457	15 042 658	12 882 639
Interest revenues, BGN thousand													
2004	96 863	194 892	299 962	406 956									299 962
2003	74 730	145 393	223 314	302 382	385 403	465 864	550 315	636 814	724 416	816 202	908 081	1 012 487	223 314
Current profit/loss, BGN thousand													
2004	41 497	78 677	114 157	132 792									114 157
2003	98 482	122 770	125 420	148 232	180 278	218 487	242 268	266 588	293 663	322 514	355 375	379 817	125 420
Social policy and industrial relations													
Wage&Salary [3)]													
Average Monthly Wage&Salary of employees under labor contract, total, nominal, BGN													
2004	279	278	292										283
2003	270	265	280	272	280	274	276	273	286	276	286	302	272
Average Monthly Wage&Salary of employees under labor contract, public sector, nominal, BGN													
2004	327	321	350										333
2003	308	299	325	318	340	327	326	324	352	326	344	368	311
Average Monthly Wage&Salary of employees under labor contract, private sector, nominal, BGN													
2004	251	253	259										254
2003	238	234	242	244	242	241	244	242	245	245	249	260	238
Real Average Monthly Wage&Salary of employees under labor contract, total, growth, corresponding period of the previous year =100, %													
2004	-2.9	-1.6	-1.8										-2.1
2003	5.7	4.9	5.8	3.6	2.3	2.1	1.3	-0.5	1.4	-1.5	0.1	1.4	5.5
Real Average Monthly Wage&Salary of employees under labor contract, public sector, growth, corresponding period of the previous year =100, %													
2004	-0.3	0.7	1.4										0.6
2003	7.3	4.7	7.1	6.4	5.1	3.8	3.4	0.3	3.5	-1.7	2.6	4.9	6.4

(Continued and end)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1
Real Average Monthly Wage&Salary of employees under labor contract, private sector, growth, corresponding period of the previous year =100, %													
2004	-0.9	1.4	0.8										0.4
2003	2.1	1.9	1.8	2.3	0.8	1.3	-0.4	-0.9	-0.3	-1.2	-1.7	-1.2	2.0
Income and consumption of the households [3]													
Total income, monthly, average per person, nominal, BGN													
2004	141.26	135.56	148.66	157.40									141.8
2003	128.82	122.39	135.79	142.38	146.59	152.29	157.20	156.96	156.98	156.21	162.10	210.61	129.0
Cash income, monthly, average per person, nominal, BGN													
2004	136.41	131.91	143.04	145.02									137.1
2003	124.46	118.32	130.16	132.49	134.22	139.11	142.22	142.00	142.20	140.66	137.16	175.31	124.3
Total expenditure, monthly, average per person, nominal, BGN													
2004	140.50	131.64	142.02	156.38									138.1
2003	125.16	116.02	130.11	135.45	143.16	141.85	147.13	151.10	153.10	154.86	153.35	197.89	123.8
Cash expenditure, monthly, average per person, nominal, BGN													
2004	136.28	128.35	136.94	146.80									133.9
2003	121.08	112.26	124.88	125.95	131.40	129.67	133.18	137.00	139.27	140.36	134.95	163.62	119.4
Real total income, monthly, average per person, growth, corresponding period of the previous year =100, %													
2004	3.0	3.9	3.1	4.2									3.3
2003	11.6	7.9	7.5	8.7	5.5	11.1	12.2	6.3	2.0	3.0	7.0	2.0	8.9
Real cash income, monthly, average per person, growth, corresponding period of the previous year =100, %													
2004	3.0	4.6	3.5	3.1									3.7
2003	11.9	7.7	7.8	8.3	7.1	11.3	11.7	6.6	1.3	2.9	3.4	5.7	9.1
Real total expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %													
2004	5.5	6.4	2.8	8.8									4.8
2003	12.4	3.3	8.3	8.9	3.1	7.3	7.9	3.7	0.1	4.3	3.1	1.9	8.0
Real cash expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %													
2004	5.7	7.2	3.3	9.8									5.4
2003	12.8	3.1	8.9	8.6	4.8	7.7	7.7	4.3	-0.4	4.6	3.4	5.9	8.2

1) Excluding credits to Monetary Financial Institutions.
2) Including credits to Non-financial Public Corporations.
3) Average monthly values by quarter are calculated as simple average of monthly per capita values.

Sources: Employment Agency, Bulgarian National Bank, Ministry of Finance, National Statistical Institute and own calculations.
Acronyms:
GDP = Gross domestic product
“ - “ = Not applicable or missing data

ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FIRST HALF OF 2004

Title	**Status**	**Official Gazette**
ORDINANCE on the management of tariff quotas	New	N 1 of 6.01.2004
ORDINANCE on the approval of the type of new motor vehicles with regard to carbon dioxide emissions and fuel consumption	New	N 2 of 9.01.2004
DECREE of CoM on setting up an Economic Policy Council	Amended	N 2 of 9.01.2004
ORDINANCE on defining the types of telecommunication activities subject to individual licensing and registration under a common license	New	N 2 of 9.01.2004
ORDINANCE on categorization of railways in the Republic of Bulgaria, included in the railway structure and closing down of individual lines or sections of lines	Amended	N 2 of 9.01.2004
ACT on the State Budget of the Republic of Bulgaria for 2004	Amended	N 3 of 13.01.2004
DECISION on adoption of a National plan for allocation of the radio frequency spectrum into radio frequencies and radio bands for civil needs, for the needs of national security and defense and common use between them	New	N 3 of 13.01.2004
ORDINANCE on the rules and standards on the structure of various types of territories and structural zones	New	N 3 of 13.01.2004
ORDINANCE on the terms and procedures for allocation of quotas of export and re-export of textile products and garments of Bulgarian origin to Canada and US	Amended	N 4 of 16.01.2004
ORDINANCE on tender offering for sale and exchange of shares	New	N 4 of 16.01.2004
ORDINANCE on the access of health insured individuals to medical establishments for out-patient and in-patient care	Amended	N 4 of 16.01.2004
ACT on waters	Amended	N 6 of 23.01.2004
DECREE of CoM on fixing the prices of tobacco products of local origin and from import to the domestic market	Amended	N 6 of 23.01.2004
REGULATIONS to the Act on protection of classified information	Amended	N 6 of 23.01.2004
CUSTOMS CONVENTION on international transportation of goods under the coverage of TIR carnets (TIR Convention of 1975)	New	N 7 of 27.01.2004
DECREE of CoM for the setting up of a Coordination Council under the National plan for development and coordination of the process of preparation of program documents for participation of the Republic of Bulgaria in the Structural Funds and the Cohesion Fund of the European Union	Amended	N 8 of 30.01.2004
ORDINANCE on protection of workers against risks related to exposure to carcinogens and mutagens at work	Amended	N 8 of 30.01.2004
ORDINANCE on defining the admissible concentrations of harmful substances in the air of the working environment	Amended	N 8 of 30.01.2004
ORDINANCE on protection of workers against risks related to exposure to chemical agents at work	Amended	N 8 of 30.01.2004
ORDINANCE on the terms and procedures for changing the participation and transfer of accumulated funds of an insured individual from one fund for supplementary pension insurance in another fund, managed by another pension insurance company	Amended	N 9 of 3.02.2004
ORDINANCE on capital adequacy and liquidity of investment intermediaries	Amended	N 9 of 3.02.2004
ORDINANCE on the terms and procedures of providing the service “leased lines”	New	N 10 of 6.02.2004
ORDINANCE on marking and commercial presentation of wines, spirits and products of grapes and wine	Amended	N 10 of 6.02.2004
ORDER on the approval of a list of municipalities in which unemployment in the previous year is 50 per cent higher than the average for the country	New	N 10 of 6.02.2004
DECREE of CoM on taxation of motor vehicles import	Amended	N 11 of 10.02.2004
ORDINANCE on evaluation and classification of banks’ risk exposure and setting apart provisions for impairment losses	Amended	N 11 of 10.02.2004
ORDINANCE on the banks-depositaries under the Social Security Code	New	N 11 of 10.02.2004
ORDINANCE on substantial requirements and assessment of compliance of machines and equipment operated in the open air with regard to their noise levels	New	N 11 of 10.02.2004
TARIFF of the charges for the right of water use and/or permit for the use of a water facility	Amended	N 11 of 10.02.2004
DECREE on the organization and coordination of the preparation of the Republic of Bulgaria for accession to the European Union and accession negotiations	Amended	N 13 of 17.02.2004
DECREE of CoM on establishing a Council for European Communication	Amended	N 13 of 17.02.2004
REGULATIONS to the Concessions Act	Amended	N 13 of 17.02.2004
ORDINANCE on the procedures for identifying, collection, spending and control over the funds and of the amounts of the contributions due to the Radio-active Waste Fund	Amended	N 13 of 17.02.2004
Regional Development ACT	New	N 14 of 20.02.2004
Roads ACT	Amended	N 14 of 20.02.2004
ORDINANCE on the norms of maximum admissible quantities of pesticide residuals in foods	New	N 14 of 20.02.2004
ORDINANCE on the norms of maximum admissible concentrations of harmful substances in the atmosphere of settlements	Amended	N 14 of 20.02.2004
ORDINANCE on the rules and requirements for collection of herbs and genetic material from healing plants	New	N 14 of 20.02.2004
ORDINANCE on the norms of benzene and carbon dioxide in the atmosphere	Amended	N 14 of 20.02.2004
RULES for the activities of life-guard centers	New	N 14 of 20.02.2004

ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FIRST HALF OF 2004

Title	Status	Official Gazette
ORDINANCE on hygienic norms on maximum admissible quantities of chemical and biological pollutants in food products	Amended	N 14 of 20.02.2004
ACT on private security businesses	New	N 15 of 24.02.2004
ACT on the Ministry of Interior	Amended	N 15 of 24.02.2004
ORDINANCE on determination of the basic package of healthcare guaranteed by the NHIF budget	Amended	N 15 of 24.02.2004
ORDINANCE on the import of goods of importance for the health of the population	Amended	N 15 of 24.02.2004
ACT on wine and spirits	Amended	N 16 of 27.02.2004
DECREE of CoM on the execution of the State Budget of the Republic of Bulgaria for 2004	Amended	N 16 of 27.02.2004
REGULATIONS to the Excise Duty Act	Amended	N 16 of 27.02.2004
ORDINANCE on regulation of electricity prices	New	N 17 of 2.03.2004
ORDINANCE on the terms and procedures of defining the minimum return of assets management in the funds for supplementary mandatory pension insurance, on covering the difference to the minimum return and formation and utilization of reserves for guaranteeing minimum return	Amended	N 16 of 27.02.2004
Energy ACT	Amended	N 18 of 5.03.2004
ACT on veterinary medical activities	Amended	N 18 of 5.03.2004
Energy Efficiency ACT	New	N 18 of 5.03.2004
ACT on live-stock breeding	Amended	N 18 of 5.03.2004
ACT on the protection of new sorts of plants and breeds of animals	Amended	N 18 of 5.03.2004
ACT on the protection of plants	Amended	N 18 of 5.03.2004
Corporate Income Tax ACT	Amended	N 18 of 5.03.2004
Local taxes and charges ACT	Amended	N 18 of 5.03.2004
ACT on assistance to agricultural producers	Amended	N 18 of 5.03.2004
ORDINANCE on defining a positive medications list in the Republic of Bulgaria	Amended	N 18 of 5.03.2004
ORDINANCE on production and trade in forest reproductive materials	New	N 18 of 5.03.2004
SINGLE CLASSIFIER of administrative positions	New	N 18 of 5.03.2004
ORDINANCE on the official status of civil servants	Amended	N 18 of 5.03.2004
ORDINANCE on the requirements to the composition and structure of owner's equity (capital base) of pension insurance companies and to the minimum liquid funds of the company and its managed supplementary pension insurance funds	Amended	N 19 of 9.03.2004
ORDINANCE on packaging and packaging waste	New	N 19 of 9.03.2004
ORDINANCE on disbursement of cash compensation for unemployment	Amended	N 19 of 9.03.2004
ORDINANCE on the functions of the National social security institute on collection and distribution of mandatory social security contributions	Amended	N 19 of 9.03.2004
TARIFF of the charges collected in the system of the Ministry of Regional Development and Public Works and by regional governors	Amended	N 20 of 12.03.2004
ACT on the budget of the state social insurance for 2004	Amended	N 21 of 16.03.2004
ORDINANCE on the elements of remuneration and of income on which social security contributions are made and on the calculation of cash benefits for temporary disability and pregnancy or delivery	Amended	N 21 of 16.03.2004
NORTH ATLANTIC TREATY	New	N 22 of 18.03.2004
ORDINANCE ON OBLIGATORY INSURANCE	Amended	N 23 of 19.03.2004
ACT on the state property	Amended	N 24 of 23.03.2004
Concessions ACT	Amended	N 24 of 23.03.2004
ACT on sea areas, internal water ways and ports of the Republic of Bulgaria	Amended	N 24 of 23.03.2004
ORDINANCE on the terms and procedures for collection of vignette tolls for paid use of certain roads of the republican network for a fixed period of time	New	N 24 of 23.03.2004
DECREE of CoM on the adoption of an Ordinance on packaging and packaging waste	Amended	N 24 of 23.03.2004
ORDINANCE on the procedures for planting of new vineyards, replanting and irradication of existing ones	Amended	N 24 of 23.03.2004
ORDINANCE on border-crossing check points	Amended	N 24 of 23.03.2004
ORDINANCE on the procedures for written declaration of goods before the customs offices	Amended	N 24 of 23.03.2004
ORDINANCE on emission norms of admissible content of harmful and hazardous substances in waste water discharged in water facilities	Amended	N 24 of 23.03.2004
RULES OF PROCEDURES of the Public Procurement Agency	Amended	N 24 of 23.03.2004
ORDINANCE on pensions and insured length of service	Amended	N 25 of 26.03.2004
ORDINANCE on terms and procedures for issue of export licenses	Amended	N 25 of 26.03.2004
CRIMINAL CODE	Amended	N 26 of 30.03.2004
REGULATIONS to the VAT Act	Amended	N 26 of 30.03.2004
ORDINANCE on the structure of forests and land of the forestry stock and hunting regions in the Republic of Bulgaria	New	N 27 of 1.04.2004
CIVIL PROCEDURE CODE	Amended	N 28 of 6.04.2004

Title	Status	Official Gazette
Health Insurance ACT	Amended	N 28 of 6.04.2004
Public Procurement ACT	Amended	N 28 of 6.04.2004
Public Procurement ACT	New	N 28 of 6.04.2004
ORDINANCE on criteria, indicators and methodology of accreditation of medical treatment establishments	Amended	N 28 of 6.04.2004
ORDINANCE on production and trade in vine planting materials	New	N 29 of 9.04.2004
ORDINANCE on the central credit register of banks	Amended	N 29 of 9.04.2004
DECREE of CoM on adoption of a tariff of the charges collected by the Communications Regulatory Commission	Amended	N 31 of 16.04.2004
RULES OF PROCEDURE of the Guarantee Fund	New	N 31 of 16.04.2004
TARIFF of the charges collected by the Communications Regulatory Commission under the Telecommunications Act	New	N 31 of 16.04.2004
TARIFF of the charges collected by the Communications Regulatory Commission under the Postal Services Act and the Act on the electronic document and electronic signature	Amended	N 31 of 16.04.2004
RULES OF PROCEDURE of the Council of Ministers and its administration	Amended	N 33 of 23.04.2004
CONVENTION on access to information, involvement of the public in decision-making and access to justice on environmental issues	New	N 33 of 23.04.2004
REGULATIONS to the Act on control of foreign trade in weapons and goods and technologies of dual use	Amended	N 35 of 28.04.2004
CIVIL PROCEDURE CODE	Amended	N 36 of 30.04.2004
FOREIGN EXCHANGE ACT	Amended	N 36 of 30.04.2004
ACT on bank bankruptcy	Amended	N 36 of 30.04.2004
ACT on the restitution of ownership on forests and forestry stock land	Amended	N 36 of 30.04.2004
ACT on the cadastre and property register	Amended	N 36 of 30.04.2004
Local charges and taxes ACT	Amended	N 36 of 30.04.2004
ACT on the Judiciary	Amended	N 29 of 9.04.2004 and N 36 of 30.04.2004
ACT on the structure of the territory	Amended	N 36 of 30.04.2004
ACT on guaranteeing receivables by employees in case of bankruptcy of employer	New	N 37 of 4.05.2004
State Charges ACT	Amended	N 24 of 23.03.2004 and N 36 of 30.04.2004 and N 37 of 4.05.2004
Investments Promotion ACT	Amended	N 37 of 4.05.2004
Individual Income Taxation ACT	Amended	N 36 of 30.04.2004 and N 37 of 4.05.2004
DECREE of CoM to ensure funds for the structural reform of healthcare	New	N 37of T4.05.2004
Customs ACT	Amended	N 38 of 11.05.2004
Health Insurance ACT	Amended	N 38 of 11.05.2004
Act on state financial internal control	Amended	N 38 of 11.05.2004
CRIMINAL PROCEDURE CODE	Amended	N 26 of 30.03.2004 and N 38 of 11.05.2004
Social Security CODE-	Amended	N 38 of 11.05.2004
Audit Office ACT	Amended	N 38 of 11.05.2004
ACT on the ownership and use of farm land	Amended	N 36 of 30.04.2004 and N 38 of 11.05.2004
ACT on the restriction of administrative regulation and administrative control over economic activities	Amended	N 39 of 12.05.2004
Tourism ACT	Amended	N 39 of 12.05.2004
RULES OF PROCEDURE of the Commission for Protection of Competition	Amended	N 39 of 12.05.2004
ORDINANCE on fixing of base prices, excluded areas and constitution of right to use and right of way on forests and forest stock land	Amended	N 39 of 12.05.2004
Public Education ACT	Amended	N 40 of 14.05.2004
Investments Promotion ACT	Amended	N 40 of 14.05.2004
ORDINANCE on the procedures for issue of permits to producers of seeds and planting materials and on registration of traders in such materials	New	N 40 of 14.05.2004
ORDINANCE on the terms and procedures for issue of licenses and permits for safe use of nuclear power	New	N 41 of 18.05.2004
ORDINANCE on the terms and procedures for payment of export subsidies in case of export of agricultural products	New	N 41 of 18.05.2004

ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FIRST HALF OF 2004

Title	**Status**	**Official Gazette**
REGULATIONS to the Act on protection of farm land	New	N 41 of 18.05.2004
ORDINANCE on licenses and permits issued by the Bulgarian National Bank	Amended	N 44 of 25.05.2004
ORDINANCE on waste classification	New	N 44 of 25.05.2004
TARIFF of the charges for radio and TV broadcasting	New	N 44 of 25.05.2004
ORDINANCE capital adequacy of banks	Amended	N 44 of 25.05.2004
ORDINANCE on high exposures of banks	Amended	N 44 of 25.05.2004
DECREE of CoM of 20.12.2001 on the adoption of combined nomenclature and introduction of an Integrated Customs Tariff of the Republic of Bulgaria	Amended	N 46 of 28.05.2004
ORDINANCE on the terms and procedure for licensing of actuaries of pension insurance companies and their managed funds for supplementary pension insurance	New	N 46 of 28.05.2004
ORDINANCE on the application of the Single Classifier of administrative positions	Amended	N 46 of 28.05.2004
ORDINANCE on the terms and procedures of assessment of employees in the state administration	Amended	N 46 of 28.05.2004
SINGLE CLASSIFIER of administration positions	Amended	N 46 of 28.05.2004
REGULATIONS to the SME Act	Amended	N 47 of 1.06.2004
Higher Education ACT	Amended	N 48 of 4.06.2004
Health Insurance ACT	Amended	N 49 of 8.06.2004
DECREE of CoM on the foreign trade regime of the Republic of Bulgaria	Amended	N 50 of 11.06.2004
Labour CODE	Amended	N 52 of 18.06.2004
Civil Aviation ACT	Amended	N 52 of 18.06.2004
ACT on the protection of classified information	Amended	N 52 of 18.06.2004
Employment Promotion ACT	Amended	N 52 of 18.06.2004
ACT on restriction of administrative regulation and administrative control over economic activities	Amended	N 52 of 18.06.2004
TAX PROCEDURE CODE	Amended	N 36 of 30.04.2004 and N 38 of 11.05.2004 and N 53 of 22.06.2004
CODE OF ETHICS of state administration employees	New	N 53 of 22.06.2004
Social Security CODE	Amended	N 12 of 13.02.2004 and N21 of 16.03.2004 and N 53 of 22.06.2004
ORDINANCE on licensing of operations in the energy sector	New	N 53 of 22.06.2004
Public Procurement ACT (effective as of 1.10.2004)	Amended	N 53 of 22.06.2004
Individual Income Taxation ACT	Amended	N 53 of 22.06.2004
Corporate Income Taxation ACT	Amended	N 18 of 5.03.2004 and N 53 of 22.06.2004
VAT ACT	Amended	N 53 of 22.06.2004
Excise Duties ACT	Amended	N 53 of 22.06.2004

METHODOLOGICAL NOTES

A. GENERAL NOTES

The review of the Bulgarian economy is an authentic expert product of the Center for Economic Development, made possible mostly owing to the long experience of the Center in the field of applied studies of the economic policy and economic development of the country.

The present report on the Bulgarian economy follows the structure and content of the review established after the report on the second quarter of 2003. The objective of last year changes was to satisfy users' interest and to establish the publication as a source of reliable and comprehensive information about the economic development and the economic policy in the past months.

The review of the Bulgarian economy in the first half of 2004 contains detailed presentation of the review period, assessment of the period and subsequent trends. This time the review is not explicitly focused on one quarter of the current year. Where necessary, significant events, facts and data from periods prior to the beginning of 2004 have been highlighted. Where possible, two main types of data comparisons have been made: against the corresponding period of 2003 or against the end of 2003. Again where possible, the dynamics within the semester itself has been traced, too. At many points also the short-term trend has been outlined.

The structure of the presentation above follows two principles simultaneously. First, the strive is towards giving a more comprehensive presentation of the subject matter areas, with corresponding prioritization of the range of matters discussed. Second, the different topics and analyses reflect the experience and interests of the experts and of the Center for Economic Development as a whole

The review of Bulgaria's economy in the first half of 2004 starts with presentation of the macroeconomic dynamics discussed against the background of the following basic categories: GDP, inflation, employment and unemployment, balance of payments, foreign trade and foreign direct investments. After that the latest values of the Estat index of business climate in Bulgaria are presented and compared. The economic events in the country in the reviewed semester, which have direct or indirect effect on the competitiveness of the Bulgarian enterprises, are analyzed in the section on the enterprise policy. Such events are described in the sub-sections on encouragement of entrepreneurship, investment promotion policy, administrative and regulatory environment, effectively functioning markets, access to financing, privatization, pubic procurement regulation, combating corruption, public administration reform, preparation for the single European market, and commercial policy. In the specific Bulgarian economic environment the enterprise policy has two basic aspects – transformation, which is mostly associated with the process of privatization and liberalization of the economy, and competitive orientation, which involves the policies to achieve economic growth and competitiveness of the Bulgarian enterprises. The corresponding section of the report studies problems concerning both aspects of the Bulgarian enterprise policy.

The public finance section covers the budget implementation and the fiscal reserve dynamics, the credit ratings, the foreign and the domestic debt. The wide topic of social and healthcare policies encompasses the issues of social security, employment and unemployment, labor market policy, income and social partnership. A review is made of the current problems and condition of the healthcare reform. The environmental policy is discussed both as a specific element of the economic policy and as a factor for the economic environment.

The financial sector is presented by means of the banking system and the capital market. Then the review of a number of sectors of significant importance to the economic development of Bulgaria comes – energy, transport, high technologies and communications, tourism and agriculture. The section on regional policy outlines the political decisions, facts and events relating to the achievement of balanced and sustainable development of the regions and reduction of the disproportions between them, as well as the process of social and economic cohesion with the European Union.

The enterprise policy in the European Union is presented under the heading "In Focus" of the present report.

The annexes at the end constitute an integral part of the presentation. Annex 1 presents in detail the basic indicators in the period under review. Annex 2 contains the list of newly passed legislation and amendments to laws, which are of significant importance to the economic development of the country, and have been promulgated in the Official Gazette in the period 1 January – 22 June 2004.

The work was finally completed on 15 July 2004.

B. SOURCES

Along with the conclusions from a large number of own outputs and works, some of which are parts of assigned research projects, the experts of the Center for Economic Development have used statistical and other information and data from the following main sources:

- National Assembly
- Council of Ministers
- Ministry of Energy and Energy Resources
- Ministry of Agriculture and Forestry
- Ministry of Economy
- Ministry of Transport and Communications
- Ministry of Labor and Social Policy
- Ministry of Finance

- National Statistical Institute
- National Social Security Institute
- Employment Agency
- Agency for Small and Medium-sized Enterprises
- Privatization Agency
- Bulgarian National Bank
- Bulgarian Stock Exchange – Sofia AD
- Financial Supervision Commission
- Delegation of the European Commission
- European Union
- Eurostat
- European Bank for Reconstruction and Development
- Organization for Economic Cooperation and Development
- Official Gazette

The particular sources and publications are quoted at the respective places in the text.

C. THE ESTAT INDEX OF BUSINESS CLIMATE IN BULGARIA

The business climate survey is based on own original methodology, developed by the team of the Agency for Social and Marketing Surveys Estat and the Center for Economic Development. The more significant details are described below.

Methodology of the Sample

The survey was conducted in the period 8 – 20 April 2004 among the managers of 398 companies. The sample is a two-level panel one (at the first level the companies are divided into groups by regions, and at the second level – according to their economic sectors as per nomenclature A6 of the NSI), and it is grouped on the basis of the indices “number of employees” and “type of ownership”. The sample is a guaranteed representative one at the level of going concerns.

Methodology of the Registration

The information has been collected using the method of an inquiry at the work place. The interviews were held with the owners of the companies covered by the sample, or with persons authorized to make management decisions and to sign financial statement documents (managers, chief accountants, commercial or marketing directors).

The questionnaire contains eight substantive questions and three passport questions. The integrated index is comprised of three components. The questions from one to five inclusive comprise Component I – “General Condition of the Company”; question six – Component II – “Investment Attitudes and Corporate Strategies”; questions seven and eight – Component III – “Business Environment”.

General Description of the Index Calculation

1. Preliminary preparation

The preliminary preparation includes weighting of the data according to the indicators “economic sector” and “number of employees”, recoding and calculating values for the respective questions.

- Questions with one possible answer

The original scales are of Likert type with codes from 1 (the highest degree) to 5 (the lowest degree). Recoding is done so as to have a scale from -2 (the lowest degree) to +2 (the highest degree).

- Multiple choice questions

These questions are recoded in advance so that possible answers are located symmetrically on both sides of the neutral point (the zero).

2. Calculation of the components

The index for each question (indicator) is calculated as a weighted average value.

Weights are assigned to each indicator within a component by means of expert evaluation. The value for each component (“General Condition of the Company”; “Investment Attitudes and Corporate Strategies”; “Business Environment”) is calculated as a weighted average.

The first table above shows the values obtained for the three components and the integrated index.

3. Calculation of an integrated index

The integrated index is calculated as a weighted average of the three components. The weight for each of the components is determined by means of expert evaluation.

The Estat index of business climate assumes values from -100 to +100. The business climate condition is assessed according to the following scale, similar to the one used in the German IFO Business Climate Index:

-100 to -61	very poor
-60 to -21	poor
-20 to +20	average
+21 to +60	good
+61 to +100	very good

Interpretation

All components (with no exception), as well as the integrated index, assume values within the interval [-100, +100]. The set of tools allows to determine also the direction of the index. The difference between the values of questions Q3 (assessment of the expected condition), Q2 (assessment of the condition at a certain point in time) and Q1 (assessment of the condition during the preceding period) is applied as a criterion for determining the direction.

Beside everything aforesaid about the methodology, in many places throughout the text additional methodological and other notes and comments are given.

CENTER FOR ECONOMIC DEVELOPMENT
1408 Sofia
1 Balsha Str., bl. 9
phone: +359 2 953 4204
fax: +359 2 953 3644
e-mail: ced@ced.bg
www.ced.bg

EVENTS

Round table on the problems of enterprise policy

From left to right: R. Pinto, consultant, Investment Compact for South-East Europe; A.Fanelli, Senior Administrator, Investment Compact for South-East Europe; D. Ivanovski, Deputy Minister of Economy; G. Prohasky, Co-chair of CED Board of Trustees

The Center for Economic Development with the support of the Investment Compact for South-East Europe with OECD organized on 13 January 2004 in the premises of the Ministry of Economy a round table on South-East Europe Enterprise Policy Performance Assessment.

In 2003 the Investment Compact for South-East Europe with OECD and EBRD with the support of experts from the Center for Economic Development completed successfully the report on Enterprise Policy Performance Assessment in Bulgaria as part of the regional project South-East Europe Enterprise Policy Performance Assessment. As an outcome of the project reports were drawn up on the enterprise policies in nine countries of South-East Europe as well as a regional report which shows the place of Bulgaria in comparative terms.

The major goal of the round table was to present and discuss the conclusions and recommendations of the regional report, as well as of the report on Bulgaria, on the six key components of the business environment for the development of enterprises:

- Institutional framework for the policy towards small and medium-sized enterprises
- Legislative and regulatory framework
- Tax policy for small businesses
- Financial instruments for start-up and small businesses
- Advisory services for start-up and small businesses
- Business incubators.

The main speakers on behalf of OECD were Antonio Fanelli, Senior Administrator, Investment Compact for South-East Europe, and Ricardo Pinto, consultant, Investment Compact for

South-East Europe, and the official host of the round table was Dimitar Ivanovski (Deputy Minister of Economy).

Work group meetings of the Enterprise Forum in South-East Europe – Vienna, February 2004, and Bucharest, May 2004.

It is for the second time that the Center for Economic Development has been the implementer for Bulgaria of the project Enterprise Policy Performance Assessment in South-East Europe; EPPA 2004), which comprises a study of the enterprise policy along various dimensions for each country of the region and is assigned by OECD.

EPPA 2004 sets the objective to clarify the viewpoint of the business on the issues of economic policy in the region (unlike, for example, the European Charter on Small Enterprises that focuses on the view point of the governments).

The first work meeting was held on 1 and 2 February 2004 in Vienna where representatives of the local consultants by countries and government agencies, supporting the SME sector development in the region, together with representatives of the Investment Compact, OECD, DG Enterprise of the European Commission and EBRD discussed the methodology and edited the major methodological instrument for implementation of EPPA 2004. Mr. Petar Stankov, enterprise policy researcher of the Center for Economic Development and coordinator of the project for Bulgaria, took part in the meeting.

At the Bucharest meeting on 24 and 25 May the Enterprise working group gathered the project coordinators of each country with representatives of government administrations supporting the SME sector, representatives of the Investment Compact, OECD, DG Enterprise of the European Commission and EBRD. The local consultants made presentations based on the outcomes of the projects in each country. Opportunities were discussed for coordination of the results of EPPA 2004 and annually developed position of Bulgarian institutions on the progress of Bulgaria on the ten basic aspects of the European Charter for Small Enterprises[74].

Workshops on the problems of corporate governance

A session of the workshop on corporate governance on 2-3 February 2004.

The Center for Economic Development completed the implementation of its last project in the area of corporate governance. It continues the good traditions of research, survey and analysis of the most problematic areas of corporate governance in Bulgaria. To this end, the Center attracts the best Bulgarian experts in order to propose legislative and institutional changes, as well as practical solutions for introduction of modern corporate governance.

The project Practical steps for reform of corporate governance in Bulgaria through training of directors was implemented in September 2003 – April 2004 with the support of the Center for International Private Enterprise (Washington, D.C. USA). It

74 1. Education and training for entrepreneurship; 2. Cheaper and faster start-up; 3. Better legislation and regulation; 4. Availability of skills; 5. Improved online access; 6. Getting more out of the Single Market; 7. Taxation and financial matters; 8. Strengthening the technological capacity of small enterprises; 9. Successful e-business models and top-class small business support;. 10. Development of stronger and more effective representation of the small enterprises' interests on Union and national level.

contributed to raising the professionalism of the members of managing bodies and high level managers in selected Bulgarian public companies. As an outcome of the project we should point the training materials developed especially for the workshops within the project; the two training seminars held in February and April with a total of 35 participants; dissemination of information and knowledge on the topic via press and electronic media. Participants in the seminars were informed of the basic points of the White Paper on Corporate Governance of OECD. With the participation of representatives of the Financial Supervision Commission and journalists, case studies were discussed from the practice of disclosure of information and the obligations of directors for contacts with investors and members of the managing bodies.

Partners to the Center for Economic Development under this project were the Center for Corporate Governance with the Institute for Postgraduate Studies at the University of National and World Economy and the Industrial Capital Association in Bulgaria.

Second work meeting of the Environmental Justice Coalition

The second meeting of experts from Central and Eastern European countries organized within the project Improvement of Environmental Justice, hosted by the Center for Environmental Policy and Law with the Central European University, was held in Budapest on 13 and 14 March 2004 and had a working nature. The meeting was attended by Mrs. Daniela Petrova, expert at the Center for Economic Development.

The focus of the meeting was the devising of a legal definition of the concept environmental justice in view of its practical usage in legal acts and procedures. Parallel to this, the preparation of a publication was discussed to present specific cases in the CEE countries related to environmental injustice to be submitted to the Fourth Ministerial Conference Environment and Health in Budapest in June. The meeting laid the foundations of future cooperation between representatives of non-government organizations and initiated joint actions directed towards promotion and application of the principles of environmental justice in the context of national environmental policies and EU acquis.

The actions of the Coalition correspond to the priorities and policies on the implementation of the Aurhus Convention, ratified by Bulgariaon 16 March 2004.

Activists from environmental protection organizations and specialists in the area of environmental policy and human rights may take part in the discussion forum of the coalition at: coalition_environmentaljustice@yahoogroups.com.

Conference: Towards the Lisbon Agenda Goals: is Bulgarian Economy Competitive?

The conference Towards the Lisbon Agenda Goals : is Bulgarian Economy Competitive? was held on 30 March 2004, organized jointly by the Center for Economic Development and the British Embassy in Sofia. This was the second conference dedicated to the Lisbon Agenda. At the end of March 2001 the beginning of a joint project was laid down – annual assessment of Bulgaria's preparedness for implementation of the Lisbon objectives. The goal of the first conference was to outline the importance of the Lisbon Agenda and the need to focus the attention of the Bulgarian society on accomplishing the objectives set forth in the strategies for increasing employment and productivity rates. Then the stress was on the policy and specific measures undertaken by various ministries in implementation of the Lisbon objectives. The second conference had the task to propose to the attention of the public the assessment of the non-government sector in the face of the Center for Economic Development for the accomplishment of these goals – both within the Union and by the candidate countries.

The analysis shows that Bulgaria has good achievements in some areas of impact, but in view of the very low starting basis, the accomplished results (though relatively high on the background of the remaining EU countries, including the newly acceded ones) are rather insufficient. Despite the expected relatively high growth rate of the gross domestic product (around 5 per cent for 2004) and continuing macro-economic stability, the average income per capita will reach 32 per cent of this in EU in 2005. According to the computations made at the Center, at a 3 per cent average annual growth rate of GDP in the 25 EU Member States and 6 per cent in Bulgaria, GDP per capita in the country will present in 2010 hardly 38 per cent of the one in EU, and in 2020 – 50 per cent. Apparently, much more investments will be required for substantial restructuring of the economy that will create foundations for significantly higher growth rates and higher incomes.

According to the Lisbon Agenda, enhancement of competitiveness should be based on encouraging the process of innovations, completion of establishing the Single internal market, development of entrepreneurship and better social cohesion. In adherence to the goals and specific objectives to be resolved by the Bulgarian society, the experts of the Center focused their analyses on four main areas of impact: process of innovations, further liberalization of the market, enterprise policy and social reform. The findings of this analysis can be seen in the Center's web-site.

From left to right: G. Prohasky, Co-chair of CED Board of Trustees; H.E. Jeremy Hill, UK Ambassador to Bulgaria; A. Boshkov, Co-chair of CED Board of Trustees; D. Ivanovski, Deputy Minister of economy; Alasdair Murray, Director at the Center for European Reform, London

Foreign experts took part in the conference, too. Alasdair Murray, Director at the Center for European Reform depicted a picture of the implementation of the Lisbon Agenda in EU Member States, including the newly acceded ones. A team of Romanian researchers – Dragos Pislaru, Executive Director of the Group of Applied Economics , and Geomina Turlea, senior researcher at the Institute of World Economy, presented the findings of a similar analysis of accomplishment of the Lisbon objectives in Romania. Representatives of the Ministry of Economy, the Ministry of Labour and Social Policy, the Agency for Development of Communications and Information and Communication Technologies and of the Coordination Center for Information, Communication and Management Technologies with the CoM presented the policies of their institutions and the recent measures towards implementation of the objectives of Lisbon. During the discussions, representatives of non-government organizations, universities and government agencies shared their views and made proposals for improvement in a number of areas.

European Innovation Trend Chart

In 2003 the Center for Economic Development was invited to take part in the so-called European Innovation Trend Chart as an official correspondent for Bulgaria. The project covers all EU Member States, as well as acceding countries, and a few groups of countries outside Europe. It is of two year duration, the idea being to turn this initiative into a permanent one allowing to monitor the innovation policies and to introduce best practices. The work under the project includes preparation of four brief documents providing information on various topics related to innovation, drawing up of a country annual report on innovation development and periodic feeding of a data base with news on the same topic.

Within the framework of the project, a meeting was held on 20 and 21 April 2004 in Brussels to clarify the work of country correspondents and summarize available information by countries. The Center was represented by Mr. Georgi Mihaylov, expert. He introduced the participants in the meeting with the situation regarding the innovation policy in Bulgaria and the ideas for the future development of the innovation system currently discussed by the government. The participants discussed and then approved the parameters for developing the country reports on innovation development by countries. The reports themselves will be officially presented in the autumn of 2004.

Round tables on the problems of the Bulgarian energy sector

Iv. Shiliashki, consultant, Dr. Drumev, consultant; T. Ermenkov, Executive Director of the Energy Efficiency Agency; M. Kovachev, Minister of energy and energy resources; Al. Boshkov, Co-chair of CED Board of Trustees; Iv. Nikolov, Program Director of CED; R. Ovcharov, MP of Coalition for Bulgaria; Pl. Mandjoukov, Deputy Executive Director of Енергопроект JSC

On 27 April 2004 the Center for Economic Development together with the Ministry of Energy and Energy Resources organized a round table “The Bulgarian energy sector through the eyes of economists”. The round table had the objective to discuss topical issues in the area of export of electricity, nuclear power, gas-fired power plants as an alternative to nuclear ones and energy efficiency. Involved in the discussions of the round table were representatives of the executive and legislative branches, non-government organizations and the academia.

The second round table organized by the Center and MEER was held on 8 June 2004 under the title Technical and Economic Feasibility of Constructing MPP Belene. The participants in the round table were representatives of MEER, large energy consumers, international institutions, banking sector and non-government organizations.

More information on the presentations made at the round table can be found at the web-site of MEER: www.doe.bg. A summary of the issues discussed can also be found in the Energy section of this report.

Annual Bank Conference on Development Economics, Brussels, Belgium

On 10 and 11 May in Brussels, Belgium, Mr. Ivaylo Nikolov, Program Director of the Center for Economic Development, participated in the regular Annual Bank Conference on Development Economics – Europe (ABCDE Europe 2004). The conference is traditionally organized by the European Vice Presidency of the World Bank in Paris, and this year co-organizers were the Office of the Prime Minister of Belgium and the Ministry of Development Cooperation of Belgium.

The title of the conference was “Doha, Monterrey and Johannesburg – Are We on Track?” Presentations, discussions and workshops were attended by leaders of the World Bank (including its President, J. Wolfenson), of the European Commission (including its President,

R. Prodi and the Commissioner of Trade P. Lamy), of various universities, research institutes and centers for public policy throughout the world.
Among the various topics and events of the conference, the presentation of J. Stiglitz from the Columbia University, USA provoked special interest. In his presentation, and later in a private discussion with the representative of the Center for Economic Development, Mr. Stiglitz shared the view that tax competition among less developed countries aimed at attracting foreign investments could have negative implications on their economic development, while not necessarily bringing benefits to individual companies. Such a position provokes interest in the context of some of the discussions on topical issues of the economic policy in Bulgaria.

Detailed additional information on the conference can be found at: http://wbln0018.worldbank.org/EURVP/web.nsf/Pages/ABCDE-Europe.

The Center for Economic Development takes part for a second year now in these conferences in its capacity of a member of Researchers Alliance for Development, set up last year. This alliance was established and operates under the auspices of the World Bank, its goals cover information exchange, contacts and joint projects among researchers, politicians and every one professionally involved with various aspects of development – economic, social, educational, health, etc. At the end of the conference, a work meeting of the alliance was held in Brussels, where the representative of the Center for Economic Development participated in the sub-group on the issues of pro-poor growth.

Seminar on the problems of “small corruption”

On 12 and 13 May 2004 a seminar was held in Vidin on the subject ”Small Corruption of Border-Crossing Points Officers in Danube 21 Euro Region as a Barrier to Implementation of Cross-border Cooperation”. The seminar was organized under the project “Small Corruption of Border-Crossing Points Officers in Danube 21 Euro Region as a Barrier to Implementation of Cross-border Cooperation in the area of the town of Vidin, Bulgaria, Kalafat, Romania, and Zaichar, Serbia and Montenegro”. The project is funded by the US Agency for International Development.

The expert of the Center for Economic Development Mrs. Blenika Djelepova delivered lectures on the subject “Training in effective methods of civil and media counteraction to corruption at BCPs” and “Training in team work between journalists and civil pressure groups for application of effective methods of civil and media counteraction to corruption at BCPs.” The possibilities for joint actions of all government bodies operating at BCPs and coordination of activities between the border-crossing points in the three countries (Bulgaria, Romania and Serbia and Montenegro) were in the core of discussions. The role of civil society and media for information of the public and their common efforts towards facilitation of border regimes underlie the work plan of the project.

The experience of the Center for Economic Development in working in anti-corruption projects was shared in the discussions.

International conference on the issues of economic reforms in the European Union

On 17 and 18 May Mr. George Prohasky, Co-Chair of CED Board of Trustees, took part in the conference in Eltvil, Germany, devoted to the economic reforms in the European Union. The conference, organized by the Wilton Park Center with the Department of Trade and Industry and

The participants in the international conference, 18 May, 2004, Eltvil, Germany

the Foreign Office of UK and Deutche Bank AG, was attended by representatives of business organizations, politicians, professional associations and experts from all European countries. The objective was to analyze the economic reforms following the year 2000 in individual European countries and in the European Union as a whole with regard to accomplishing the objectives of the Lisbon Agenda. The common conclusion was that Europe is lagging behind in carrying out the reforms and additional efforts are needed to achieve the objectives of Lisbon. Such efforts should be aimed at liberalization of economies of European countries, deregulation of the labour market and social security systems, building up a single market of financial services, gradual reduction of subsidies in a number of sectors, in agriculture in particular. The US economic model was examined with its advantages demonstrated so far to the European one. These were discussed by the Undersecretary of Economic Policy at the US Treasury Department Dr. M. Warsawski. Measures undertaken by Germany to dynamize German economy were presented by the newly elected President of Bundesbank prof. A. Weber. Special attention was paid to the new Member States of EU and their role in the process of raising the competitiveness of European economy. On the Bulgarian part, the conference was attended by Mr. A. Paparizov, Vice Chair of the Economic Policy Commission of the Parliament.

International conference on the problems related to the European Union enlargement

Work session of the conference in Varna

An international conference The European Union after 1 May, 2004 – is there a shock after the enlargement? Implications for South-East Europe and the enlarged Union was held from 10 to 12 June 2004 in Varna. Organizer of the conference was the Bulgarian European Community Studies Association. Over 30 representatives of different countries took part in the presentations and discussions – old and new Member States of EU, candidate-countries for the next enlargement, countries from the region which have not yet started negotiations. Among the participants in the conference were H.E. Mihal Kotman, Ambassador of the Slovak Republic to Bulgaria, Mr. Iosip Shpoliarit, acting leader of the Croatian Embassy in Bulgaria, Prof. Dr. Jim Rollo, Director of the European Institute to the Sussex University, UK, Prof. Dr. Atila Eralp, Director of the Center for European Studies at the Middle East Technical University, Ankara, Prof. Dr. Irena Kikerkova from the University of Skopjie, Prof. Dr. Irji Melih from Carlton University, Ottawa, and many Bulgarian experts, professors and researchers.

The Center was represented by Mrs. Marieta Tzvetkovska, Senior Expert. She gave a presentation titled "Bulgaria and the enlarged EU – before we step over the threshold of membership". Parallel to outlining the advantages and risks of the current enlargement for the country, special attention was paid to the challenges posed by the enlarged EU in relation to the proper structuring of the economic policy for the accomplishment of the goals of successful accession, deepening of cooperation with Romania as an acceding country and encouraging partnership in the Balkans to assist Balkan countries in their preparation for membership in the Union.

Meeting of the public policy centers in Chisinau, Moldova

From 17 to 19 June 2004, in Chisinau, Moldova, Mr. Ivaylo Nikolov, Program Director of the Center for Economic Development, took part in the regular work meeting of the network of public policy centers from Eastern Europe and the countries of former Soviet Union, supported by the Open Society Institute.

In the first day a seminar was held on the topic “Policy Entrepreneurship”. The centers from Eastern Europe and ex-Soviet Union were introduced with the experience of representatives of the London-based Overseas Development Institute with regard to development and efficient implementation of public policies, as well as the interaction between research and public policy. Presentation of practical case studies on the work organization of analytical centers for public policy was followed by a more general discussion on the theory and practice of various mechanisms and approaches to analysis of the context, development of the policy and achieving effects with its implementation.

The second day of the meeting in Moldova was fully devoted to the practical issues of institutionalization of the network of public policy centers in the region. Based on documents prepared by the working group on establishment of the future association, the topics discussed covered the goals and objectives of the association, statutes, membership, registration, funding and name. The necessary decisions were discussed and voted which now makes possible the formal registration and establishment of the association. The city of Prague was selected as the base and the name of the association will be “Policy Association for an Open Society”, or abbreviated – PASOS.

Charter against Corruption

A session of the public discussion on preparation of the Charter against Corruption on 25 March 2004 at Velingrad.

An Anti-corruption Forum was held on 18 June 2004 in Velingrad where for the first time in the country an Charter against Corruption was signed.

The creation of this document, unique for Bulgaria, was initiated under the project of the Center for Economic Development “Involvement of Business in a More Efficient Fight against Corruption in Velingrad Municipality”. The project is implemented under the program “Civil Society against Corruption” of Coalition 2000 with the financial support of USAID. The local partner under the project is the Regional Development Agency – Velingrad. The major goal of the project, that is being implemented over the period January – September 2004, is to build up sustainable mechanisms for prevention of corruption through public/private partnership between local authorities, business and civil society. The following basic activities were carried out under the project by June:

- Two focus groups were held in February with the participation of representatives of institutions, civil and religious societies, local entrepreneurs and business people of various economic sectors. Subject of vivid discussions were the reasons for existence and spreading of corruption, the significance of the problem for the municipality and initiatives to curtail it, the idea of signing an Anti-corruption Charter.
- A public discussion was held in March attended by representatives of the local government, including the Mayor, the Chair of the Municipal Council, municipal councilors, representatives of business organizations, state authorities, non-government organizations, media. Subject

The Charter against Corruption is open for signing, Velingrad, 18 June 2004

of the discussions were the major findings in the report of sociologists on focus groups with a stress on identification and typology of corrupt practices in the municipality, as well as the possibilities to lower public tolerance to corruption. The expected advantages of the municipality were presented – creating favourable environment to attract investments. The meeting elected an expanded Civil Initiative Committee (CIC) to devise the Charter against Corruption.

- In April and May CIC at its sessions approved the wording of the Charter and prepared the anti-corruption forum in June.
- In June a special Internet application of the Charter was developed and activated at: www.cbivel.org.

The event of 18 June was attended by many citizens and visitors to Velingrad, the Member of Parliament Panaiot Liakov, the Secretary of the Commission for Coordination of the Activity for Combat with Corruption to the CoM Konstantin Palikarski, the Deputy Regional Governor Yumer Hamza, representatives of branch organizations, NAMRB, non-government organizations, USAID Open Government Initiative Project, media. Mr. Thomas Peebles, Resident Legal Advisor , US Embassy, expressed on behalf of H.E. the Ambassador of US James Pardew the support of the US Government and its Embassy in Sofia to the efforts to curtail corruption in Bulgaria, as well as the entire approval of the project. Special letters in support to the idea of the Charter against Corruption were received at the Center for Economic Development from Mrs. Lydia Shouleva, Deputy Prime-Minister and Minister of Economy, Mr. Nikola Filtchev, Prosecutor General, Miroslav Sevlievski, MP, Bojidar Danev, President of BIA.

The Charter is an open document and every one who accepts its principles may join it. It can be signed in the Town hall and in the Business and Information Center, Velingrad.

Following the Ant-corruption Forum the guests of the event attended a presentation at the Business and Information Center on the topic "Velingrad – Economic Potential and Investment Prospects".

Round Table "Economic Relations between Russia and Bulgaria – Old Glory and New Opportunities"

A session of the Round Table "Economic Relations between Russia and Bulgaria – Old Glory and New Opportunities"

A round table was held on 29 June 2004 in Sofia jointly organized by Overgas AD and the Center for Economic Development dedicated to the issues of trade and economic relations between Russia and Bulgaria. It was attended by representatives of the President's Office – Ertan Kara, Secretary on economic issues, of the Government – Meglena Kuneva, Minister of European Affairs, and Radoslav Bozadjiev, Deputy Minister of Economy, of the state administration (FIA, MoE), academic circles (the Institute of Economics with BAS), the non-government sector (BIA, the European Institute, Bulgarian-Russian Chamber of Commerce) and of the business.

The contemporary economic relations between Russia and Bulgaria and the new realities in which they are developing

Meglena Kuneva, Minister of European Affairs, and S. Donchev, Executive Director of Overgas at the round table "Economic Relations between Russia and Bulgaria – Old Glory and New Opportunities"

are a subject of interest to both the business and researchers. The organizers of the round table had the objective to bring together representatives of various circles to discuss the issues and opportunities of bilateral cooperation and to outline specific problems and addressees for their resolution. The negotiations between Russia and EU and WTO were examined as a foundation for contemporary bilateral relations. Official statistics about the commodities exchange served as a starting point to define the role and importance of relations with Russia.

The participants in the discussion concluded that a long-term program needs to be elaborated for the development of economic relations between Bulgaria and Russia which should not only outline the directions but to also offer specific measures in various areas of bilateral cooperation and priorities in resolving the problems of leading exporters. Such a program could be developed on the level of business associations (chambers of commerce) with the involvement of research institutes. To this end, additional discussions are to be organized and studies conducted on individual aspects of Bulgarian-Russian relations and the cooperation of the non-government sector should be sought, as well as of all forms of business and other associations, alliances, organizations of individuals demonstrating interest to the development of bilateral relations.

MEETINGS "ON THE ROOF"

Meeting "On the roof" with H.E. Baroness Henriette van Lynden, Ambassador of the Kingdom of Netherlands to Bulgaria

In 2004 again the leadership of the Center for Economic Development continued the initiative to organize meetings "On the roof". These are informal gatherings in the Roof Hall to which the Center invites diplomats, representatives of the state administration, leading economic experts and representatives of different political parties. At these meetings the expert staff of the Center and its guests discuss topical economic, political and social problems and share their views for the development of the Bulgarian economy.

During the period January – June 2004 the Center was visited by H.E. Baroness Henriette van Lynden, Ambassador of the Kingdom of Netherlands to Bulgaria, the new Resident Representative of UNDP, Bulgaria Mr. Neil Buhne, Mr. Stamen Tassev, Deputy Minister of Finance, in charge of the Customs Agency, the General Tax Directorate, the National Revenue Agency, Tax Policy Directorate and European Integration and Monitoring Directorate, and H.E. Yasuyoshi Ichihashi, Ambassador of Japan.

Meeting "On the roof" with Mr. Neil Buhne (the first on the right) Resident Representative of UNDP, Bulgaria

Meeting "On the roof" with H.E. Yasuyoshi Ichihashi, Ambassador of Japan (the second on the left)

NEW PUBLICATIONS

In May 2004 the book “Towards the Lisbon Agenda Goals : Is Bulgarian Economy Competitive?” was published.

The publication is based on the materials of the international conference held in Sofia on 30 March 2004 and organized jointly by the British Embassy in Sofia and the Center for Economic Development.

The publication contains a summary of the report of the European Commission before the spring European Council of 2004, an analysis by the experts of the Center for Economic Development of the accomplishment of the objectives in Bulgaria, presentations at the conference by representatives of the state administration and foreign participants from British and Romanian research institutes, as well as the major points of the discussions held.

In June the White Paper on Corporate Governance in South-East Europe, OECD, 2003, was published. It is the result of the debates held at the Round table on corporate governance in South-East Europe and contains a range of recommendations to improve corporate governance practices and the respective supporting institutional framework in the countries of the region. It is addressed to politicians, economists, financiers, investors, professors and students. The five chapters of the White Paper discuss the following issues: rights and fair treatment of shareholders; the role of stakeholders; transparency and disclosure of information; responsibilities of corporate boards; application of enforcement measures.

The preparation for the publication in Bulgarian of the White Paper is made by a team of the Center for Economic Development and the Center for Corporate Governance at the Post-Graduate Qualification Institute with the University for National and World Economy – Maria Prohaska Ph.D. and professor Bistra Boeva Ph.D. Thus, one of the recommendations of the White Paper itself was fulfilled – its dissemination and presentation before the business circles, the public and the state administration in Bulgaria.